see vol. - 7463

No. 11547

United States

Circuit Court of Appeals

For the Ninth Circuit.

COMMISSIONER OF INTERNAL REVENUE,

Petitioner,

vs.

RAINIER BREWING COMPANY,
A Corporation,

Respondent.

Transcript of Record

In Five Volumes

Volume I

Pages 1 to 190

Upon Petitions to Review a Decision of the Tax Court of the United States.

FILED

MAY 17 1947

Rotary Colorprint, 870 Brannan Street, San Francisco

PAUL P. O'BRIEN,

No. 11547

United States
Circuit Court of Appeals
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COMMISSIONER OF INTERNAL REVENUE,

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

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APPEARANCES:

For Taxpayer:

A. CALDER MACKEY, ESQ.,

ARTHUR McGREGOR, ESQ.,

HOWARD W. REYNOLDS, ESQ.,

ADAM Y. BENNION, ESQ.,

SCOTT H. DUNHAM, ESQ.,

F. SANFORD SMITH, ESQ.

For Commissioner:

B. H. NEBLETT, ESQ. [1*]

* Page numbering appearing at top of page of original certified Transcript of Record.

Docket No. 4895

RAINIER BREWING COMPANY,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

DOCKET ENTRIES

1944

May 12—Petition received and filed. Taxpayer notified. Fee paid.

May 13—Copy of petition served on General Counsel.

June 9—Answer filed by General Counsel.

June 9—Request for hearing in San Francisco, California, filed by General Counsel.

June 15—Notice issued placing proceeding on San Francisco, Calif., calendar. Service of answer and request made.

1945

Feb. 10—Hearing set April 23, 1945, in San Francisco, California.

Mar. 21—Hearing date changed to 7/9/45 in San Francisco, California.

June 16—Motion to amend petition, amendment to petition lodged, filed by taxpayer, 6/19/45 Granted.

June 19—Copy of motion and amendment served on General Counsel.

July 19—Hearing had before Judge Harron on merits. Three stipulation of facts and answer to amended petition, filed and served. Petitioner's original brief due 9/24/45. Comm'rs brief 11/8/45. Petitioner's reply 12/10/45.

Aug. 13—Transcript of hearing 7/19/45 filed.

Aug. 13—Transcript of hearing 7/20/45 filed.

Aug. 13—Transcript of hearing 7/21/45 filed.

Sept. 20—Motion for extension of 30 days to file brief, filed by taxpayer. Granted.

Oct. 22—Brief filed by taxpayer. 10/23/45 Copy served.

Nov. 28—Motion for extension to 1/23/46 to file brief, filed by General Counsel. 11/29/45 Granted.

Dec. 31—Motion to file the attached brief as amici curiae, filed by H. B. Jones, and A. R. Kehoe. 1/14/46 Granted.

1946

Jan. 14—Brief of amici curiae filed by H. B. Jones and A. R. Kehoe.

Jan. 23—Motion for extension to 2/23/46 to file brief, filed by General Counsel. 1/24/46 Granted.

Feb. 25—Brief filed by General Counsel. Served 2/26/46.

Mar. 25—Motion for extension to 4/26/46 to file reply brief filed by taxpayer. 3/26/46 Granted.

1946

Apr. 29—Motion for leave to file the attached reply brief, filed by taxpayer. 4/29/46 Granted.

Apr. 29—Reply brief filed by taxpayer. 5/2/46 Served.

June 18—Findings of fact and opinion rendered, Judge Harron. Decision will be entered under Rule 50. Copy served 6/19/46.

June 24—Notice of appearance of Adam Y. Bennion, Scott H. Dunham, and F. Sanford Smith as counsel filed. (3)

July 26—Respondent's computation for entry of decision filed.

July 29—Hearing set 9/11/46 on settlement. Washington, D. C.

Aug. 2—Hearing date changed to 8/14/46.

Aug. 7—Consent to respondent's computation filed.

Aug. 12—Decision entered. Judge Harron. Div. 13.

Nov. 5—Petition for review by U. S. Circuit Court of Appeal, 9th Circuit, filed by General Counsel.

Nov. 14—Proof of service of notice of filing petition for review filed by G. C. on taxpayer.

Nov. 18—Proof of service of notice of filing petition for review filed by General Counsel on A. Calder Mackay, Esq.

Dec. 6—Certified copy of order from the 9th Circuit extending time to 2/15/47 to prepare and transmit the record, filed.

1947

Jan. 21—Statement of points filed with statement of service thereon.

Jan. 21—Designation of portions of record to be printed filed with statement of service thereon.

Jan. 21—Designation of contents of record filed with statement of service thereon. [2]

The Tax Court of the United States

Docket No. 4895

RAINIER BREWING COMPANY,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION

The above-named petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency (symbols IRA:90-D LB) dated March 9, 1944, and as a basis of its proceeding alleges as follows:

I.

The petitioner is a corporation organized and existing under and by virtue of the laws of the State of California, with its principal office and place of business in the City and County of San

Francisco, California. The returns for the periods here involved were filed with the Collector of Internal Revenue for the First District of California, at San Francisco, California.

II.

The notice of deficiency (a copy of which is attached and marked "Exhibit A") was mailed to the petitioner on March 9, 1944.

III.

The taxes in controversy are income and declared value excess-profits taxes for the calendar year 1940 in the respective amounts of $235,321.78 and $18,617.60, and excess-profits taxes for the calendar years 1940 and 1941 in the respective amounts of $285,948.74 and $26,119.92. [3]

IV.

The determination of tax set forth in the said notice of deficiency is based upon the following errors:

(a) The Commissioner erred in determining that promissory notes in the principal amount of $1,000,000.00 received by petitioner during the calendar year 1940 constituted ordinary income, and in failing to determine that said notes constituted the proceeds from the sale in the year 1940 of petitioner's trade names, brands and good will in the State of Washington and the Territory of Alaska.

(b) The Commissioner erred in failing to de-

termine that the said trade names, brands and good will sold by petitioner in 1940 had a basis equal to or in excess of the value of the said notes received in exchange therefor and that there was no taxable gain derived by the petitioner from said sale.

(c) The Commissioner erred in treating the said notes as income or gain subject to tax under the Internal Revenue Code, inasmuch as the income or gain, if any, reflected by said notes was attributable to and had accrued during the period prior to March 1, 1913, and it was not the intent or purpose of Congress to tax the realization of such income or gain.

(d) In the alternative and if it be held that the said notes are taxable as ordinary income, the Commissioner erred in failing to allow petitioner a deduction for the year 1940 of at least the same amount by reason of the exhaustion in said year of the economic usefulness to petitioner of its trade names, trade brands and labels of "Rainier" and "Tacoma" within the State of Washington and the Territory of Alaska.

(e) The Commissioner erred in failing to determine that the major part of the amount of said notes constituted abnormal income attributable to years prior to 1940 within the meaning of section 721 of the Internal [4] Revenue Code, and consequently he erred in determining a deficiency in excess-profits tax for the year 1940.

(f) The Commissioner erred in reducing petitioner's excess-profits credit for the years 1940 and

1941 by deducting from base period net income for the calendar year 1938 the sum of $23,677.52.

V.

The facts upon which the petitioner relies as the basis of this proceeding are as following:

(a) Petitioner is a corporation organized and existing under and by virtue of the laws of the State of California, with its principal office and place of business in the City and County of San Francisco, California. For many years, i.e., since 1893 (except during the period of prohibition), petitioner and its predecessors have been engaged in the business of manufacturing and marketing beer, ale and other alcoholic malt beverages, which products have been sold and distributed principally under the trade names and brands of "Rainier" and "Tacoma".

(b) Seattle Brewing & Malting Company, a Washington corporation, was organized in the year 1893. It established its principal offiec and place of business in the City of Seattle, State of Washington, and built a brewery in Georgetown, Seattle, where it manufactured and sold beer, ale and other alcoholic malt beverages under the "Rainier" label.

(c) In the year 1899 the said predecessor corporation (Seattle Brewing & Malting Company) registered the trade name "Rainier" in the United States Patent Office, and further registrations of said trade name were obtained in the years 1907, 1914 and 1915. The trade name "Rainier" was

also duly registered in the State of Washington. Said registrations have been continued in full force and effect to the present time. In the year 1903 [5] said Seattle Brewing & Malting Company caused a new corporation to be organized under the laws of the State of West Virginia, under the name of Seattle Brewing and Malting Co., which acquired all the assets of the predecessor corporation. In the same year a corporation was organized under the laws of the State of Washington, known as Rainier Brewing Company, in order further to protect the name "Rainier".

(d) Said Seattle Brewing & Malting Company and its immediate successor, Seattle Brewing and Malting Co., manufactured, at the brewery in Georgetown, Seattle, beer, ale and other alcoholic malt beverages under the trade name "Rainier", using such labels as "Rainier Beer", "Rainier Pale Beer", and "Rainier Bock Beer", during the period from 1893 until the year 1915, when the State of Washington enacted a law prohibiting the manufacture and sale of alcoholic malt beverages in that State. During the period of such operations the companies' products were sold and distributed principally in the State of Washington; a market was also developed for such products in Oregon, California, and other Pacific slope states and the Territory of Alaska. In the year 1915 Seattle Brewing and Malting Co. acquired a site and built the Rainier Brewery in San Francisco, where beer, ale and other alcoholic malt beverages were manufactured and marketed under the said "Rainier"

trade names and trade labels until national prohibition went into effect in the year 1920. For several years thereafter near-beer and other non-alcoholic malt beverages were manufactured and distributed by said last-mentioned corporation, under labels bearing the trade mark "Rainier".

(e) In the year 1925 a reorganization of Seattle Brewing and Malting Co. (the West Virginia corporation) and Rainier Brewing Company (the Washington corporation) was effected whereby said corporations transferred to Pacific Products, Inc., a California corporation, organized in 1925 for that purpose, the brewery plant and property in San Francisco, and also the brewery plant and property in Georgetown, Seattle, Washington, together with all the business, good will, trade names, trade marks, and labels owned and used by Seattle Brewing and Malting Co. and Rainier Brewing Company (the Washington corporation). Thereafter, and until September, 1932, Pacific Products, Inc., continued to manufacture and distribute, at the San Francisco plant, non-alcoholic malt beverages and carbonated beverages, using labels bearing the trade mark "Rainier", such as "Rainier Lager", "Rainier Old German Lager", "Rainier Malt Tonic", "Rainier Ginger Ale", and "Rainier Lime Rickey". In the year 1927, Pacific Products, Inc., acquired the business of the Tacoma Brewing Company in San Francisco, including the trade name, trade mark, and brand of "Tacoma", and thereafter marketed some of its products under the "Tacoma" label.

(f) In the year 1932, when it was anticipated that the prohibition law would be repealed and the manufacture and sale of real beer would again be legalized, a new corporation, with the name of Rainier Brewing Company, Inc., was organized under the laws of the State of California. Said corporation acquired the brewery plants and properties in San Francisco, California, and Georgetown, Seattle, Washington, formerly operated by Seattle Brewing and Malting Co., Rainier Brewing Company, and Pacific Products, Inc., together with the good will, business, trade names, trade marks, brands and labels owned and used by those companies. When repeal of prohibition became effective in the year 1933 said Rainier Brewing Company, Inc., commenced the manufacture, sale and distribution of beer, ale and other alcoholic malt beverages, principally under the "Rainier" trade names and labels owned by it, and to a lesser degree under the trade name and label of "Tacoma". Said corporation also qualified to do business in a number of states, including [7] Oregon and Washington, and in the Territory of Alaska. It established an office and distributing plant at the site of the original brewery in Georgetown, Seattle, Washington, from which beer, ale and other alcoholic malt beverages were sold and distributed in the State of Washington and the Territory of Alaska.

(g) On March 1, 1913, the principal sales territory for said products was the State of Washington, and the fair market value on that date of the sole and exclusive right to manufacture and

market beer, ale and other alcoholic malt beverages within the State of Washington and the Territory of Alaska under the trade name, brand and label of "Rainier" was, as petitioner is informed and believes, at least the sum of $1,000,000.00.

(h) Under date of April 23, 1935, petitioner's immediate predecessor, Rainier Brewing Company, Inc. (of which petitioner is successor through a statutory merger or consolidation), entered into a written contract with Century Brewing Association, a Washington corporation hereinafter known as Century, whereby the latter was granted the exclusive right and license to manufacture and market within the State of Washington and the Territory of Alaska beer, ale and other alcoholic malt beverages under the trade names, trade marks, and labels of "Rainier" and "Tacoma", in consideration of the payment of royalties at the rate of 75c per barrel for all such products sold, up to 125,000 barrels, with a minimum royalty of $75,000.00 per annum, and 80c per barrel for every barrel of product sold under said trade names and brands in excess of 125,000 barrels per annum; such royalties to be payable quarterly on January 1, April 1, July 1, and October 1 of each year.

(i) Pursuant to the terms of said contract, Rainier sold to Century its brewery plant located at Seattle, Washintgon, together with the [8] beer on hand and personal property situated at said brewery, and Rainier withdrew from the sale and distribution of its products in the State of Washington and the Territory of Alaska.

(j) During the five years following the execution of said contract, Century manufactured and marketed in the State of Washington and the Territory of Alaska beer, ale and other alcoholic malt beverages under the trade name and brand of "Rainier". Century did not market any products under the trade name and brand of "Tacoma". During said five years, Century paid to Rainier Brewing Company, Inc. and to petitioner the royalties as called for in said contract, and the amount of said royalties was included in the gross income for Federal income tax purposes of Rainier and petitioner.

(k) During the year 1940 Century exercised the option granted to it by said contract and delivered to petitioner promissory notes in the principal amount of $1,000,000.00, as a lump sum payment for the exclusive and perpetual right and license thereafter to manufacture and market beer, ale and other alcoholic malt beverages within the State of Washington and the Territory of Alaska under the Trade names and brands of "Rainier" and "Tacoma".

(l) As a consequence of the exercise of said option by Century, petitioner, in the year 1940, disposed finally and definitively of its trade names, brands and good will in the State of Washington and the Territory of Alaska, and of its sole and exclusive right to manufacture and market beer, ale and other alcoholic malt beverages within the State of Washington and the Territory of Alaska under the trade names, brands and labels of "Rainier" and "Tacoma". Petitioner realized no

taxable gain or income from said transaction, by virtue of the fact that the right thus sold or otherwise disposed of had, as petitioner is informed and believes, a basis equal to or in excess [9] of the fair market value of the notes received in exchange therefor.

(m) During the calendar year 1938 petitioner abandoned certain neon signs purchased by it in 1935. The unrecovered cost of such neon signs at the time of abandonment was $23,386.92, which sum was deducted by petitioner on its Federal income tax return for 1938 as a loss due to abandonment. The said deduction was allowed by the Commissioner as claimed on the return. In computing excess-profits net income for the year 1938 the Commissioner erroneously and illegally refused to treat the said loss as a loss due to abandonment and determined that said loss represented ordinary and necessary business expense for the year 1938.

Wherefore, the petitioner prays that this Court may hear the proceeding and redetermine the aforesaid deficiencies in accordance with the rights of the petitioner in the premises and grant such other and further relief, including refunds, as to it may seem just and proper as a result of such redetermination.

Dated: April 29, 1944.

/s/ A. CALDER MACKAY,
/s/ ARTHUR McGREGOR,
/s/ HOWARD W. REYNOLDS,
Counsel for Petitioner. [10]

State of California,
City and County of San Francisco—ss.

F. S. Smith, being duly sworn, deposes and says: That he is Secretary of Rainier Brewing Company, the petitioner named in the foregoing petition; that he is duly authorized to verify said petition; that he has read the said petition and knows the contents thereof; that the same is true of his own knowledge, except as to those matters which are therein stated on information or belief, and as to those matters he believes it to be true.

F. S. SMITH.

Subscribed and sworn to before me this 4th day of May, 1944.

(Notarial Seal) JAMES F. McCUE,

Notary Public in and for said City and County of San Francisco, State of California. [11]

EXHIBIT A

Treasury Department
Internal Revenue Service
74 New Montgomery Street
San Francisco 5, California

Mar. 9, 1944.

Office of Internal Revenue Agent in Charge San Francisco Division
IRA:90-D
LB

Rainier Brewing Company
1550 Bryant Street
San Francisco, California

Gentlemen:

You are advised that the determination of your income tax liability for the taxable year ended December 31, 1940 discloses a deficiency of $235,-321.78 and an overassessment of $5,791.97 for the taxable year ended December 31, 1941; that the determination of your declared value excess-profits tax liability for the taxable year ended December 31, 1940, discloses a deficiency of $18,617.60 and that the determination of your excess profits tax liability for the taxable years ended December 31, 1940, and December 31, 1941, disclose a deficiency of $312,068.66 as shown in the statement attached.

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiency or deficiencies mentioned.

Within 90 days (not counting Sunday or a legal

holiday in the District of Columbia as the 90th day) from the date of the mailing of this letter, you may file a petition with The Tax Court of the United States, at its principal address, Washington, D. C., for a redetermination of the deficiency or deficiencies.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Internal Revenue Agent in Charge, San Francisco 5, California, for the attention of Conference Section. The signing and filing of this form will expedite the closing of your return(s) by permitting an early assessment of the deficiency or deficiencies, and will prevent the accumulation of interest, since the interest period terminates 30 days after filing the form, or on the date assessment is made, whichever is earlier.

Respectively,

JOSEPH D. NUNAN, JR.,
Commissioner,

By /s/ F. M. HARLESS,
Internal Revenue Agent
in Charge.

Enclosures:
Statement
Form of waiver. [12]

STATEMENT

San Francisco
IRA :90-D
LB

Rainier Brewing Company,
1550 Bryant Street,
San Francisco, California

Tax Liability for the Taxable Years Ended
December 31, 1940 and December 31, 1941

Year	Liability	Assessed	Overassessment	Deficiency
Income Tax				
1940	$387,232.14	$151,910.36		$235,321.78
1941	217,686.12	223,478.09	$5,791.97	
Totals	$604,918.26	$375,388.45	$5,791.97	$235,321.78
Declared Value Excess-Profits Tax				
1940	$ 18,617.60	—		$ 18,617.60
Excess Profits Tax				
1940	$285,948.74	—		$285,948.74
1941	27,413.19	$ 1,293.27		26,119.92
Totals	$313,361.93	$ 1,293.27		$312,068.66

In making this determination of your tax liability, careful consideration has been given to your protest of November 15, 1943 and to the statements made at the conference held on December 16, 1943 and subsequent dates.

The overassessment of income tax shown herein will be made the subject of a certificate of overassessment which will reach you in due course through the office of the collector of internal revenue for your district, and will be applied by that official in accordance with section 322, Internal Revenue Code, provided that you fully protect yourself against the running of the statute of limitations with respect to the apparent overassessment referred to in this letter, by filing with the collector of internal revenue for your district a claim for refund on form 843, a copy of which is enclosed, the basis of which may be as set forth herein.

A copy of this letter and statement has been mailed to your representative, Mr. Scott H. Dunham, Crocker Building, San Francisco, California, in accordance with the authority contained in the power of attorney executed by you and on file in this office. [13]

Adjustments to Net Income

Year: 1940

Net income as disclosed by return	$ 633,179.76
Unallowable deductions and additional income:	
(a) Income under royalty contract	1,000,000.00
Total	$1,633,179.76
Nontaxable income and additional deductions:	
(b) Capital stock tax	875.00
Net income adjusted	$1,632,304.76

Explanation of Adjustments

(a) In the taxable year you received a payment of $1,000,000.00 from the Century Brewing Association under a contract executed in 1935 whereby you granted to Century Brewing Company a license to use trade names, held by you, in connection with the marketing of beer, ale, and other alcoholic liquors made from malt, in the State of Washington and the Territory of Alaska. No income from such payment was reported in your return for 1940. You contend that the receipt of $1,000,000.00 represented the proceeds of a sale by you of good will and an interest in the trade names; that such good will and trade names have a basis, represented by the market value at March 1, 1913, in excess of the proceeds; that hence no deductible loss was allowable and no taxable gain was reportable. It is held that the contract executed in 1935 did not affect a sale of trade names or good will; that the payment of $1,000,000.00 received by you in 1940 was ordinary income taxable in full without any offset for the claimed basis.

It is further held that since the transaction did not constitute a sale, the income realized in 1940 may not be excluded from excess profits net income under section 721 of the Internal Revenue Code.

(b) The allowable deduction for capital stock tax accrued is revised as follows:

Declared value of capital stock at December 31, 1940 as shown in return filed for year ended June 30, 1941	$9,500,000.00
Capital stock tax accrued July 1, 1940 at rate of $1.25 per $1,000.00 of declared value	11,875.00
As deducted in return	$ 11,000.00
Increased allowance	$ 875.00

Computation of Declared Value Excess-Profits Tax
Year: 1940

Net income for declared value excess-profits tax computation		$1,632,304.76
Less:		
10 percent of $13,500,000.00, value of capital stock as declared in your capital stock tax return for the year ended June 30, 1940	$1,350,000.00	
Dividends received credit (85 percent of $258.75)	219.94	1,350,219.94
Balance subject to declared value excess-profits tax		$ 282,084.82
5 per cent of declared value of capital stock		675,000.00
Balance		0
Amount taxable at 6 percent $282,084.82		$ 16,925.09
Declared value excess-profits defense tax (10 percent of $16,925.09)		1,692.51
Total declared value excess-profits and declared value excess-profits defense taxes assessable		$ 18,617.60
Declared value excess-profits tax assessed:		
Original, April 1941 account No. 410350—First California District		None
Deficiency of declared value excess-profits tax		$ 18,617.60

Computation of Income Tax

Year: 1940

Net income for declared value excess-profits tax computation		$1,632,304.76
Less:		
Declared value excess-profits tax		18,617.60
Adjusted net income		$1,613,687.16
Less:		
Dividends received credit		219.94
Normal tax net income		$1,613,467.22
Income tax (22.1 percent of $1,613,467.22)		$ 356,576.26
Income defense tax (1.9 percent of $1,613,467.22, normal tax net income)		30,655.88
Total income and income defense taxes assessable		$ 387,232.14
Income tax assessed:		
Original, April 1941 account No. 410350—First California District		151,910.36
Deficiency of income tax		$ 235,321.78

Adjustments to Excess Profits Net Income as Computed Under the Income Credit Method

Year: 1940

Excess profits net income as disclosed by return		$ 480,517.12
Additions:		
(a) Net addition to normal-tax net income as shown herein		999,125.00
Total		$1,479,642.12
Deductions:		
(b) Declared value excess-profits tax	$ 18,617.60	
(c) Additional income tax	235,321.78	253,939.38
Excess profits net income as revised		$1,225,702.74

Explanation of Adjustments

(a) The net addition to normal-tax net income is explained in the foregoing.

(b) Declared value excess-profits tax as revised herein	$ 18,617.60
As shown in return	0
Increased allowance	$ 18,617.60
(c) Income tax as revised herein	$ 387,232.14
As shown in return	151,910.36
Increased allowance	$ 235,321.78

Adjustments of Excess Profits Credit Based on Income

Year: 1940

	As disclosed by return	Additions (Deductions)	Corrected
Base Period Net Income			
Excess profits net income			
Year ended December 31, 1936	$(15,221.28)		$(15,221.28)
Year ended December 31, 1937	(12,871.12)		(12,871.12)
Year ended December 31, 1938	166,589.74	(a)$(23,677.52)	142,912.22
Year ended December 31, 1939	629,204.72		629,204.72
Totals	$767,702.06		$744,024.54
Net aggregate	782,923.34		759,345.82
Average base period net income—General average	195,730.83		189,811.45

Base Period Net Income—
Increased Earnings in Last Half

Net aggregate, last half of period	$ 772,116.94
Net aggregate, first half of period	28,092.40
Excess, last half over first half	$ 800,209.34
50 percent of such excess	$ 400,104.67
Add: Net aggregate for last half	772,116.94
Total	$1,172,221.61

Average Base Period Net Income

Based on above	$ 586,110.80
Amount limited to excess profits net income for year ended December 31, 1939	$ 629,204.72
Excess Profits Credit—95 percent of average base period net income	$ 556,805.26
Excess Profits Credit—Based on Income	$ 556,805.26

Explanation of Adjustment

(a) Base period net income for the year ended December 31, 1938 is decreased by $23,677.52, as shown below:

1. To restore deduction for obsolescence eliminated on the return as abnormal income	$23,386.92
2. Additional deduction for State franchise tax	290.60
Net additional deductions	$23,677.52

1. No elemination of abnormal deduction for obsolescence is allowable for charges for Neon beer signs. Such items represent normal advertising expense.

2. Further reduction in 1938 income is made for additional franchise taxes applicable to such year, paid in 1940.

Computation of Excess Profits Tax

Year: 1940

Excess profits net income		$1,225,702.74
Less:		
Specific exemption	$ 5,000.00	
Excess profits credit	556,805.26	561,805.26
Adjusted excess-profits net income		$ 663,897.48
Tax on $ 20,000.00 at 25 percent		$ 5,000.00
Tax on 20,000.00 at 30 percent		9,000.00
Tax on 50,000.00 at 35 percent		17,500.00
Tax on 150,000.00 at 40 percent		60,000.00
Tax on 250,000.00 at 45 percent		112,500.00
Tax on 163,897.48 at 50 percent		81,948.74
Total excess profits tax		$ 285,948.74
Total excess profits tax assessable		$ 285,948.74
Excess profits tax assessed:		
Original, Account No. 801759—First California District		—
Deficiency of excess profits tax		$ 285,948.74

Adjustments to Net Income

Year: 1941

Net income as disclosed by return		$ 723,184.85
Unallowable deductions and additional income:		
(a) Taxes, real estate	$2,075.36	
(b) Beer Tax	5,377.50	
(c) Refund California Unemployment Insurance	1,142.04	
(d) State franchise tax	35.00	8,629.90
Total		$ 731,814.75
Nontaxable income and additional deductions:		
(e) Capital stock tax		1,193.75
Net income adjusted		$ 730,621.00

Explanation of Adjustments

(a) Real property taxes in the amount of $2,075.36 were paid in the taxable year on property purchased in July 1941. Such taxes were a lien on the property at time of purchase and constitute part of the purchase price. No deductions therefor are allowable.

(b) In 1939 additional beer taxes in the amount of $10,615.00 were asserted against you by the Federal Government. Such additional taxes were claimed and allowed to you as a deduction on your return for 1939. The liability for such taxes was later compromised and in 1941 a settlement payment was made in the amount of $5,237.50 leaving a balance of $5,377.50 unpaid of the amount previously accrued and deducted. It is held that the balance unpaid after the final settlement in 1941 represents income taxable in such year.

(c) The deduction for California Unemployment taxes accrued and paid in the year 1941 is reduced in the amount of $1,142.04 determined to be an overpayment and refunded to you in 1942.

(d) Due to the reduction in net income for the year 1940 for the overstatement of capital stock taxes in the amount of $875.00 for such year, the allowable deduction for California State franchise tax accrued in 1941 on the basis of net income for 1940, is reduced in the amount of $35.00, being the applicable rate of 4 percent for franchise tax applied against $875.00. No additional deduction is

allowed for franchise tax applicable to the increase of $1,000,000.00 in reportable net income for the year 1940, since you deny that any franchise tax liability was incurred in connection with such alleged income.

(e) The allowable deduction for capital stock tax accrued in 1941 is revised as follows:

Declared value of capital stock on December 31, 1941, as shown in return filed for the year ended June 30, 1942		$12,000.000.00
Capital stock tax accrued July 1, 1941 at rate of $1.25 per $1,000.00 of declared value	$	15,000.00
Amount deducted in your return		13,806.25
Additional deduction allowable	$	1,193.75

Computation of Declared Value Excess-Profits Tax

Year: 1941

Net income for declared value excess-profits tax computation		$ 730,621.00
Less:		
10 percent of $9,500,000.00, value of capital stock as declared in your capital stock tax return for the year ended June 30, 1941	$950,000.00	
Dividends received credit	188.06	950,188.06
Balance subject to declared value excess-profits tax		None
Total declared value excess-profits tax assessable		None
Declared value excess-profits tax assessed:		
Original, Account No. 411100—First California District		None

Computation of Income Tax

Year: 1941

Net income for declared value excess-profits tax computation		$730,621.00
Less: Declared value excess-profits tax		None
Net income for capital stock tax purposes		$730,621.00
Less: Excess-profits tax as revised herein		27,413.19
Adjusted net income		$703,207.81
Less: Dividends received credit		188.06
Normal-tax net income		$703,019.75
Normal Tax Computation		
Normal-tax net income	$703,019.75	
Tax at 24 percent on $703,019.75		$168,724.74
Surtax Computation		
Surtax net income	$703,019.75	
Tax at 6 percent on $ 25,000.00	$ 1,500.00	
Tax at 7 percent on 678,019.75	47,461.38	48,961.38
Total normal tax and surtax		$217,686.12
Total income tax assessable		$217,686.12
Income tax assessed:		
Original, Account No. 411100—First California District		223,478.09
Overassessment of income tax		$ 5,791.97

Adjustments to Excess Profits Net Income as Computed Under the Income Credit Method

Year: 1941

Excess profits net income as disclosed by return	$722,429.75
Additions:	
(a) Net additions to normal tax net income as shown herein	7,436.15
Excess profits net income as revised	$729,865.90

Explanation of Adjustments

(a) The net additions to normal-tax net income are explained in the foregoing.

Adjustments of Excess Profits Credit Based on Income

Year: 1941

	As disclosed by return	Additions (Deductions)	Corrected
Base Period Net Income			
Excess profits net income:			
Year ended December 31, 1936	$(10,867.73)		$(10,867.73)
Year ended December 31, 1937	(8,991.09)		(8,991.09)
Year ended December 31, 1938	188,421.08	(a) $(22,734.95)	164,686.13
Year ended December 31, 1939	749,634.51		749,634.51
Totals	929,064.50		$905,329.55
Average base period net income—General average	$222,266.12		$226,332.39

Base Period Net Income—
Increased Earnings in Last Half

Net aggregate, last half of period	$ 914,230.64
Net aggregate, first half of period	(19,858.82)
Excess, last half over first half	$ 934,179.46
50 percent of such excess	467,089.73
Add: Net aggregate for last half	914,320.64
Total	$1,381,410.37

Average Base Period Net Income Based on above		$ 690,705.18
Amount limited to excess profits net income for year ended December 31, 1939		$ 749,634.51
Excess Profits Credit—95 percent of average base period net income		656,169.92
Excess Profits Credit—Based on Income		$ 656,169.92

Explanation of Adjustments

(a) The base period net income for the year ended December 31, 1938 is reduced by $23,734.95, deduction for obsolescence. No elimination of abnormal deduction for obsolescence is allowable for charges for Neon beer signs. Such items represent normal advertising expense.

Computation of Excess Profits Tax

Year: 1941

Excess profits net income		$729,865.90
Less:		
Specific exemption	$ 5,000.00	
Excess profits credit	656,169.92	661,169.92
Adjusted excess profits net income		$ 68,695.98
Tax on $20,000.00 at 35 percent		$ 7,000.00
Tax on 30,000.00 at 40 percent		12,000.00
Tax on 18,695.98 at 45 percent		8,413.19
Total excess profits tax assessable		$ 27,413.19
Excess profits tax assessed:		
Original, account No. 400549—First California District		1,293.27
Deficiency of excess profits tax		$ 26,119.92

Received and filed May 12, 1944. [23]

[Title of Tax Court and Cause.]

ANSWER

Comes now the Commissioner of Internal Revenue, respondent above named, by his attorney, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, and for answer to the petition filed by the above-named petitioner, admits and denies as follows:

I.

Admits the allegations contained in paragraph I of the petition.

II.

Admits the allegations contained in paragraph II of the petition.

III.

Admits the allegations contained in paragraph III of the petition.

IV

Denies that the determination of tax set forth in the notice of deficiency is based upon errors as alleged in subparagraphs (a) to (f), inclusive, of paragraph IV of the petition.

V.

(a) Admits the allegations contained in subparagraph (a) of paragraph V of the petition.

(b) Admits the allegations contained in subparagraph (b) of paragraph V of the petition.

(c) Admits that in the year 1899 the predecessor corporation (Seattle Brewing & Malting Company) registered the trade name "Rainier" in the United States Patent Office, and further registrations of said trade name were obtained in the years 1907, 1914 and 1915; admits that the trade name "Rainier" was also duly registered in the State of Washington; admits that said registrations have been continued in full force and effect to the present time; admits that in the year 1903 said Seattle Brewing & Malting Company caused a new corporation to be organized under the laws of the State of West Virginia, under the name of Seattle Brewing and Malting Co., which acquired all the assets of the predecessor corporation; denies that in the same year a corporation was organized under the laws of the State of Washington, known as Rainier Brewing Company, in order further to protect the name "Rainier".

(d) Admits the allegations contained in subparagraph (d) of paragraph V of the petition.

(e) Admits that in the year 1925 a reorganization of Seattle Brewing and Malting Co. (the West Virginia corporation) and Rainier Brewing Company (the Washington corporation) was effected whereby said corporations transferred to Pacific Products, Inc., a California corporation, organized in 1925 for that purpose, the brewery plant and property in San Francisco, and also the brewery plant and property [25] in Georgetown, Seattle, Washington, together with all the business, good will, trade names, trade marks, and labels owned

and used by Seattle Brewing and Malting Co. and Rainier Brewing Company (the Washington corporation); admits that thereafter, and until September, 1932, Pacific Products, Inc., continued to manufacture and distribute, at the San Francisco plant, non-alcoholic malt beverages and carbonated beverages, using labels bearing the trade mark "Rainier", such as "Rainier Lager", "Rainier Old German Lager", "Rainier Malt Tonic", "Rainier Ginger Ale", and "Rainier Lime Rickey"; for lack of information denies that in the year 1927, Pacific Products, Inc., acquired the business of the Tacoma Brewing Company in San Francisco, including the trade name, trade mark, and brand of "Tacoma", and thereafter marketed some of its products under the "Tacoma" label.

(f) Admits that in the year 1932 a new corporation was organized under the laws of the State of California; for lack of information denies the remaining allegations contained in subparagraph (f) of paragraph V of the petition.

(g) Denies the allegations contained in subparagraph (g) of paragraph V of the petition.

(h), (i), (j), and (k) Admits the allegations contained in subparagraphs (h), (i), (j), and (k) of paragraph V of the petition.

(l) and (m) Denies the allegations contained in subparagraphs (l) and (m) of paragraph V of the petition. [26]

VI.

Denies generally and specifically each and every allegation in the petition not hereinbefore admitted, qualified, or denied.

Wherefore, it is prayed that the Commissioner's determination be approved and the petitioner's appeal denied.

/s/ J. P. WENCHEL, TMM
Chief Counsel, Bureau of
Internal Revenue.

Of Counsel:

B. H. NEBLETT,
Division Counsel.

T. M. MATHER,
Special Attorney,
Bureau of Internal Revenue.

TMM/ls 6/3/44

Received and filed June 9, 1944. [27]

[Title of Tax Court and Cause.]

AMENDMENT TO PETITION

The petition in the above entitled cause is hereby amended in the following particulars:

1. By amending paragraph IV(e) to read as follows:

> "(e) The Commissioner erred in failing to determine that the face amount of said notes, or, in the alternative, the major portion thereof, constituted abnormal income attributable to years other than the taxable year 1940 within the meaning of section 721 of the

Internal Revenue Code, and consequently he erred in determining a deficiency in excess profits tax for the year 1940."

2. By amending paragraph V(1) by adding at the end thereof a new sentence as follows: [28]

"The property thus sold or otherwise disposed of constituted capital assets which had been held by petitioner for more than 18 months."

/s/ A. CALDER MACKAY,
/s/ ADAM Y. BENNION,
Counsel for Petitioner.

Of Counsel:

/s/ F. SANFORD SMITH,
/s/ CLIFFORD J. MacMILLAN,
/s/ O. J. SONNENBERG,
/s/ SCOTT H. DUNHAM. [29]

State of California,
City and County of San Francisco—ss.

F. S. Smith, being duly sworn, deposes and says: That he is Secretary of Rainier Brewing Company, the petitioner named in the foregoing amendment to petition; that he is duly authorized to verify said amendment to petition; that he has read the said amendment to petition and knows the contents thereof; that the same is true of his own knowledge, except as to those matters which are therein stated on information or belief, and as to those matters he believes it to be true.

F. S. SMITH.

Subscribed and sworn to before me this 8th day of June, 1945.

(Notarial Seal) JAMES F. McCUE,

Notary Public in and for said City and County and State.

Lodged June 16, 1945.

[Endorsed]: Filed and motion granted June 19, 1945. [30]

[Title of Tax Court and Cause.]

ANSWER TO AMENDMENT TO PETITION

Comes now the Commissioner of Internal Revenue, by his attorney, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, and for answer to the amendment to the petition filed by the above-named petitioner, and denies as follows:

1. Denies that the Commissioner erred as alleged in paragraph 1 of the amendment to the petition.
2. Denies the allegations contained in paragraph 2 of the amendment to the petition.

/s/ J. P. WENCHEL, BHN
Chief Counsel, Bureau of Internal Revenue.

Of Counsel:

B. H. NEBLETT,
Division Counsel,
Bureau of Internal Revenue.

BHN/vg

Filed July 23, 1945. [31]

[Title of Tax Court and Cause.]

FINDINGS OF FACT AND OPINION

1. The amount received by petitioner in 1940 for the exclusive and perpetual right to use its trade names in a limited territory held not ordinary income, but proceeds from the sale of a capital asset. Seattle Brewing & Malting Co., 6 T. C. 856.

2. The March 1, 1913, value of good will incident to trade names determined.

3. Held, deduction for loss in value of good will occasioned by the National Prohibition Amendment is not provided for by the words "exhaustion" or "obsolescence" as used in the income tax laws and is neither "allowed" nor "allowable" within the meaning of section 113 (b) (1) (B) of the Internal Revenue Code. Clarke v. Haberle Crystal Springs Brewing Co., 280 U. S. 384. Therefore, such loss "allowed" by the Commissioner is limited to the tax benefits realized by the taxpayer.

4. Held, an agreement not to compete executed in 1935 had no ascertainable value in 1940.

A. Calder Mackay, Esq., Adam Y. Bennion, Esq., F. Sanford Smith, Esq., and Scott H. Dunham, C. P. A., for the petitioner.

B. H. Neblett, Esq., for the respondent.

The respondent determined deficiencies in income tax, declared value excess profits tax, and excess profits tax for the years 1940 and 1941 as follows:

	Year	Deficiency
Income tax	1940	$235,321.78
Declared value excess profits tax	1940	18,617.60
Excess profits tax	1940	285,948.74
	1941	26,119.92

Petitioner contests the determination made by the respondent. Petitioner contends that $1,000,000 of promissory notes which it received in the taxable year 1940 did not constitute ordinary income, as respondent has determined. Petitioner contends that it received the notes as the consideration for the sale of its trade names, brands, and trade-marks in the State of Washington and the Territory of Alaska. [32]

There are four questions to be decided in this proceeding. The first question is whether there was a sale of a capital asset. If there was a sale of a capital asset, a second question must be determined, namely, the amount of the gain or loss, which, in turn, requires our determination of the basis of the capital asset as of March 1, 1913. Petitioner contends that no gain was realized because it attributes a March 1, 1913, value to the property involved of more than $1,000,000, the amount of the consideration received in 1940. The third question relates to the adjusted basis of the property which was sold. The fourth question is whether any part of the $1,000,000 which petitioner received in 1940 is allocable to an agreement not to compete which was contained in the contract of April 23, 1935.

The issue with respect to the excess profits tax for the year 1941 in the amount of $26,119.92 has been abandoned by the petitioner, so that the deficiency for 1941 is $26,119.92.

The case is submitted on the pleadings, certain stipulations, and oral and documentary evidence submitted at the hearing.

Findings of Fact

The petitioner is a corporation, organized under the laws of the State of California, with its principal office and place of business in the city and county of San Francisco, California. The income tax returns for the periods here involved were filed with the collector of internal revenue for the first district of California at San Francisco, California.

Petitioner's predecessor in interest, Seattle Brewing & Malting Co. (sometimes hereinafter referred to as Seattle), was incorporated under the laws of the State of Washington in 1893. Its principal place of business was in Seattle, where it built a brewery and manufactured beer, ale, and other alcoholic malt beverages for sale under the trade name and brand of "Rainier."

In 1903 a new corporation by the name of "Seattle Brewing and Malting Co." (also referred to hereinafter as Seattle) was organized under the laws of West Virginia. This corporation acquired all the assets of the Washington corporation, including the trade name "Rainier," and operated the business until the end of 1915 when, because of

statewide prohibition, it stopped the manufacture of beer and ale in the State of Washington and began manufacturing these products at San Francisco, California, through its wholly owned subsidiary, Rainier Brewing Co., a Washington corporation, until national prohibition went into effect in 1920.

In 1925 Seattle and its wholly owned subsidiary, Rainier Brewing Co., were merged through a nontaxable reorganization into a California [33] corporation known as Pacific Products, Inc., which was organized in 1925 for that purpose. This company acquired all the assets of the two former companies, which included the plants in Seattle and San Francisco, together with their assets, business, good will, trade-marks, trade names, and labels. In 1927 Pacific Products, Inc., acquired by purchase the right to use the trade name "Tacoma." Pacific Products, Inc., operated the business until 1932 when, through a nontaxable reorganization, "Rainier Brewing Co., Inc.," a California corporation organized in 1932, acquired all the assets of Pacific Products, Inc. (except certain designated assets not used in the conduct of its manufacturing business) including the trade names "Rainier" and "Tacoma." In 1937 Rainier Brewing Co., Inc., was merged into the Pacific Products, Inc., in a nontaxable reorganization, and Pacific Products, Inc., as the surviving company, changed its name to Rainier Brewing Co., the petitioner herein.

Rainier Brewing Co., Inc., carried on the busi-

ness that had been conducted by its predecessor, and with the repeal of prohibition in 1933 resumed the manufacture and sale of real beer, ale, and other alcoholic malt beverages under the trade name "Rainier." Such products were manufactured at the plant in San Francisco. The plant in Seattle was only used as a warehouse and sales office for distribution of the products in the State of Washington.

In view of the rapid expansion of business following the repeal of prohibition the officers of Rainier Brewing Co., hereinafter referred to as petitioner, in about the year 1935 considered reopening the Seattle plant as a brewery. About that time, however, they were approached by a competing company in the State of Washington, known as the Century Brewing Association (hereinafter referred to as Century), with a view to acquiring the right to use the trade names "Rainier" and "Tacoma" in the manufacture and sale of beer in the State of Washington and the Territory of Alaska and to have the name Seattle Brewing & Malting Co.

The trade name "Rainier" had a well established and recognized value by reason of its use and development and Century was desirous af acquiring the right to use it in connection with the manufacture and sale of its own beer. The trade name "Tacoma" was less used and was not so valuable.

As a result of negotiations a contract was entered into between petitioner and Century on April 23, 1935, under which Century purchased certain prop-

erty and equipment located in Seattle and certain personal property, and secured the right to use the trade names "Rainier" and "Tacoma" in the State of Washington and the Territory of Alaska (hereinafter sometimes referred to as Washington) in [34] consideration of the payment of certain sums to be determined on a production basis or a minimum royalty specified therein.

The contract of April 23, 1935, after reciting the mutual desire of petitioner to sell and Century to purchase petitioner's Seattle plant and certain personal property located in Seattle and the State of Washington, and of Century to secure by royalty contract and of petitioner to grant the right to use the trade names "Rainier" and "Tacoma," within the State of Washington and the Territory of Alaska, and after providing in detail for the sale of the physical properties, continues with the following provisions:

Licensing Agreement

Seventh: Rainier hereby grants to Century the sole and exclusive perpetual right and license to manufacture and market beer, ale and other alcoholic malt beverages within the State of Washington and the Territory of Alaska under the trade-names and brands of "Rainier" and "Tacoma" together with the right to use within said State and Territory any and all copyrights, trademarks, labels, or other advertising media adopted or used by Rainier in connection with its beer, ale, or other alcoholic malt beverages.

Eighth: In consideration of said perpetual right and license, Century agrees to pay to Rainier in cash, lawful money of the United States, a royalty amounting to seventy-five cents (75c) per barrel (consisting of 31 gallons) for every barrel of beer, ale, or other alcoholic malt beverages sold or distributed in the State of Washington and the Territory of Alaska under the said trade names or brands of "Rainier" and "Tacoma" up to a total of one hundred twenty-five thousand (125,000) barrels annually, and eighty cents (80c) per barrel for all such products distributed within said territory annually in excess of said amount of one hundred twenty-five thousand (125,000) barrels; provided, however, that the minimum annual amount to be so paid by Century to Rainier shall be the sum of seventy-five thousand dollars ($75,000.00), which said amount is herein termed "minimum annual royalty." Said payments shall be made in lawful money of the United States as follows:

* * * * * * *

Century further agrees that annually on the 1st day of August of each year, commencing with the 1st day of August, 1936, it will deliver to Rainier a statement prepared by Price, Waterhouse & Co., or other Certified Public Accountants acceptable to Rainier, showing the sales of beer, ale and other alcoholic malt beverages under the trade names or brands of "Rainier" and "Tacoma" for the contract year commencing July 1st and ending June

30th immediately preceeding the date of such statement.

Rainier shall have the right, at its own cost and expense, to examine the books, records and accounts of Century for the purpose of verifying any such statement so submitted to determine the accuracy thereof.

Ninth: Rainier agrees that during the period of time this agreement remains in force, it will not manufacture, sell or distribute, within the territory herein described, directly or through or by any subsidiary company or instrumentality wholly owned or substantially controlled by it, beer, ale, or other alcoholic malt beverages, or directly or indirectly enter into competition with Century in said territory. It is understood and agreed, however, that Rainier shall have the sole and exclusive right to manufacture, sell, and distribute non-alcoholic beverages [35] within said territory under said trade names or brands of "Rainier" and "Tacoma" and any and all other trade names or brands that it owns and desires to use.

Rainier agrees that during the period of time this agreement remains in force it will maintain in full force and effect Federal registration of said trade names or brands, "Rainier" and "Tacoma," and will likewise maintain in full force and effect the present registration of said trade names or brands within the State of Washington and Territory of Alaska. Should Rainier fail to so maintain its rights under said trade names or brands, then and

in that event Century shall have the right to pay any and all amounts necessary to so maintain said trade names or brands for and in the name of Rainier, and shall be entitled to deduct any and all amounts so paid from the royalties then due or thereafter becoming due under this agreement.

Tenth: Century agrees that any and all beer, ale, or other alcoholic malt beverages manufactured by it pursuant to this agreement and marketed under said trade names and brands of "Rainier" and "Tacoma" shall at all times be of a quality at least equal to the quality of similar products then manufactured and marketed under said trade names and brands by Rainier; and shall be manufactured under the same formulae used in the manufacture of similar products by Rainier, which formulae Rainier shall make available to Century.

Eleventh: It is understood and agreed by and between the parties hereto that should Century at any time be prevented from manufacturing, selling, and distributing beer, ale, or other alcoholic malt beverages due to strikes, boycotts, fires, earthquakes or acts of God, for periods of time in excess of three (3) months, and as a result thereof Century shall fail to earn a sufficient amount from the operation of its entire business to enable it to pay the royalty next due and payable under this agreement, then and in that event, the time of payment of such royalty shall be deferred for a period of time equal and equivalent to the period during which such cause shall continue, but in no event

beyond a date upon which Century has available sufficient funds to pay royalty payments that have accrued; provided, however, that during any such period when royalty payments shall be so deferred, Century shall apply all of its monthly net income derived from the operation of its entire business toward the payment of any royalties so due.

Should the citizens residing in any portion of the territory covered by this agreement elect to adopt local prohibition laws prohibiting the manufacture, sale, and distribution of beer, ale, or other alcoholic malt beverages in such community, and should Century, due to such laws, be unable to sell and distribute within the territory described in this agreement, beer, ale, and other alcoholic malt beverages manufactured under the trade-names and brands of "Rainier" and "Tacoma" in a quantity at least equal to fifty-two thousand (52,000) barrels annually, then and in that event, the minimum royalty payable hereunder shall be reduced during the continuance of the operation of such laws by the percentage that the sales of such products under such trade names and brands of "Rainier" and "Tacoma" sold within that particular community bear to the total sales of such products by Century under such brands within the entire territory covered hereby, which percentage shall be based upon the average sales of such products theretofore made hereunder.

It is further understood and agreed by and between the parties hereto that should Century at any

time be prevented from manufacturing, selling and distributing beer, ale, or other alcoholic malt beverages under the brands and trade names of "Rainier" and "Tacoma," in a quantity at least equal to fifty-two thousand (52,000) barrels annually, due to governmental action, war regulation, [36] or general prohibitory laws adopted by the United States of America or the State of Washington, then and in that event Century shall have the option of terminating this agreement or submitting to arbitration, in the manner hereinafter provided, the question of adjusting the minimum royalties payable hereunder during the continuance of such restriction upon the operation of its business. In the event that Century elects to submit the matter to arbitration, it agrees to abide by any decision rendered by the arbiters, and to pay the minimum royalties so fixed, in the manner and at the times herein provided. Rainier agrees, in the event of such arbitration, to accept the royalties so fixed in satisfaction of the obligation of Century for such period.

Twelfth: Century agrees that upon acquiring title to the real property herein agreed to be sold to it by Rainier, it will, in addition to executing the mortgage provided in paragraph Third hereof, execute and deliver to Rainier such document or documents as Rainier shall deem necessary to cause said real property to stand as security for the prompt and faithful compliance by Century of all of its obligations under this agreement, to the end that should Century default in the performance of its obligations under this agreement and should

Rainier elect to terminate this agreement, then and in that event, title to said real property shall pass to Rainier, free and clear of all liens and encumbrances, as and for liquidated damages due to such default.

Century further agrees that should it sell said property, it will, under written agreements satisfactory to Rainier, impound the proceeds received from such sale to the extent of two hundred fifty thousand dollars ($250,000.00), or such sums as shall be realized on said sale, which said impounded funds shall thereafter stand as security for the prompt and faithful compliance by Century of all of its obligations under this agreement, and in the event of default, be transferred and delivered to Rainier as and for liquidated damages.

It is understood and agreed by and between the parties hereto that in the event of the default of Century hereunder, the termination of this agreement by Rainier, and the transfer or delivery to Rainier of said real property, or such impounded proceeds as liquidated damages, Rainier shall, in addition thereto, be entitled to recover any and all royalties due and payable under this agreement at the time of the termination thereof, which said amounts Century agrees to pay upon demand.

Thirteenth: It is understood and agreed by and between the parties hereto that at any time after this agreement has been in force for five (5) years, Century shall have the right and option of electing to terminate all royalties thereafter payable here-

under by notifying Rainier of its election so to do, and by executing and delivering to Rainier the promissory notes of Century aggregating in principal amount the sum of one million dollars ($1,000,000.00) dated as of the date of the exercise of such option, bearing interest from date at the rate of five per cent (5%) per annum, which said promissory notes shall be divided into five (5) equal maturities and shall be payable respectively on or before one (1), two (2), three (3), four (4), and five (5) years after the dates thereof.

Paragraphs fourteenth to twenty-fifth were headed "Miscellaneous Provisions." In paragraph fourteenth Century agreed to purchase from petitioner at prevailing market prices all malt required in the manufacture of beer, ale, and other alcoholic malt beverages under the trade names and brands of "Rainier" and "Tacoma." In paragraph fifteenth Century agreed to use its best efforts to increase the sales of alcoholic malt beverages within its territory and to expend in [37] advertising amounts equal to those expended in advertising all other beverages manufactured and sold by it under other brands in Washington. In paragraph seventeenth petitioner agreed to cause the old "Seattle Brewing and Malting Company," the West Virginia corporation, to change its name to the end that Century might adopt the name "Seattle Brewing & Malting Company." Paragraph twenty-second provided that if Century should fail to fully and promptly carry out the terms and provisions of the agreement or to make payments according thereto after proper

notice by petitioner, such failure should be considered an event of default and petitioner should cancel the agreement by written notice to Century, in which event all the rights of Century should terminate and liquidated damages as specified in paragraph twelfth would accrue to petitioner. It was further provided in paragraph twenty-fourth that the agreement should be binding upon and inure to the benefit of the parties and their respective successors and assigns, provided, however, that no rights of Century should be assigned by it without the written consent of petitioner first had and obtained.

The contract was carried into execution. In pursuance of paragraph seventeenth of the agreement Century changed its name from Century Brewing Association to "Seattle Brewing & Malting Company" (sometimes hereinafter referred to as either Century or the purchaser). Petitioner withdrew from the sale and distribution of its alcoholic malt products in Washington. The Seattle plant was deeded by petitioner to Century and Century conveyed the Seattle plant to a bank as trustee and executed its trust indenture with petitioner as beneficiary, all in accordance with the terms of the agreement. From time to time thereafter various amendments were made to the contract of April 23, 1935, none of which substantially affected the provisions respecting the use of the trade names.

Thereafter Century operated under the licensing

agreement until July 1, 1940, and royalties paid pursuant thereto were claimed and allowed as deductions for income tax purposes. During the period from June 30, 1935, to July 1, 1940, Century sold alcoholic malt beverages in Washington and the Territory of Alaska under the name of "Rainier" in quantities set out below and paid "royalties" thereon as follows:

Year ended June 30—	Barrels sold	Royalties paid
1936	60,171.51	$75,000.00
1937	82,881.50	75,000.00
1938	114,308.16	85,731.12
1939	112,538.17	84,403.63
1940	131,355.59	98,834.47
Total	501,254.93	418,969.22

On July 1, 1940, Century exercised the option granted to it in paragraph thirteenth of the agreement and executed and delivered to petitioner promissory notes in the aggregate amount of $1,000,000, bearing interest at 5 per cent and payable on five equal maturity dates of one, two, three, four, and five years, respectively, thereafter. These notes were made payable to petitioner. Note No. 1, in the amount of $200,000, was paid on its due date July 1, 1941. Notes Nos. 2 and 3, for $200,000 each, payable on July 1, 1942, and July 1, 1943, respectively, were paid in 1942. In consideration for the advance payment petitioner granted to Century, subject to all the terms and conditions of the contract of April 23, 1935, the "sole and perpetual right and license" to manufacture and market alcoholic malt bever-

ages within the State of Idaho under the trade names and brands "Rainier" and "Tacoma" without any payment therefor other than the payment of the remaining promissory notes given by Century in settlement of all royalty payments under the agreement of April 23, 1935.

In the fall of 1942 Century arranged to pay in advance the notes of July 1, 1944, and July 1, 1945, in the principal amount of $200,000 each, together with interest thereon, less $10,000 of such interest, in consideration of petitioner (1) releasing the properties held by the First National Bank of Seattle, as trustee, from the lien thereon and directing the conveyance of such property to Century; (2) releasing the provisions in the contract of April 23, 1935, for the purchase of malt from petitioner; and (3) amending the contract of April 23, 1935, so as to permit the manufacture and sale of beer under the trade names of "Rainier" and "Tacoma" to any plant or plants owned or controlled by Century within the States of Idaho and Washington and the Territory of Alaska without the necessity of securing the written consent of petitioner in connection therewith.

Aside from the changes indicated above as consideration for advance payment of the notes and accrued interest thereon, no changes were made in the contract of April 23, 1935, after the election by petitioner to exercise the right to "terminate the payment of all royalties" by the payment of $1,000,000.

Upon the exercise of the option and the execution and delivery to petitioner of its promissory notes aggregating $1,000,000, Century acquired the perpetual and exclusive right to manufacture and market beer, ale, and other alcoholic malt beverages within the State of Washington and the Territory of Alaska without any further payments and without regard for the amount of alcoholic malt beverages so manufactured and sold.

By the exercise of the option, as provided in paragraph thirteenth of the contract, and the payment of the consideration of $1,000,000, [39] Century acquired the exclusive and perpetual right to manufacture and sell alcoholic malt beverages in the designated territory under the trade names "Rainier" and "Tacoma." This transaction constituted the sale and acquisition of a capital asset.

From the time of its organization in 1893 to 1915 the predecessor of petitioner had brewery and manufacturing facilities located at Seattle in the State of Washington. In the fall elections of November 1914 the State of Washington adopted prohibition, effective January 1, 1916, and in 1915 Seattle, a predecessor of petitioner, moved its manufacturing business from the State of Washington to the State of California, where it built a brewery at San Francisco and removed thereto all of the brewing machinery from its Washington plant, except the cold storage facilities. After 1915 the plant in Seattle was not operated as a brewery, but was used

for storage of "Rainier" products which were shipped from San Francisco for sale in the State of Washington. These products during the era of national prohibition consisted of near beer containing one-half of one per cent alcohol.

Upon the repeal of prohibition in 1933 petitioner began the sale of "Rainier" beer and other alcoholic malt beverages in the State of Washington under the trade name "Rainier," which it continued until 1935, when it entered into the agreement under which Century acquired the exclusive and perpetual right to manufacture and sell alcoholic malt beverages under the trade names "Rainier" and "Tacoma" in the State of Washington and the Territory of Alaska and petitioner agreed not to compete with Century in the sale of alcoholic malt beverages under these trade names in the limited territory designated in the agreement.

From 1908 (and prior thereto) until 1913 a predecessor of petitioner sold alcoholic malt beverages under the trade name "Rainier" in the States of Washington, Montana, Nevada, Arizona, California, and Oregon, and also exported beer to the Orient, Central America, Honolulu, and South America.

In the State of Washington during the period 1908 to 1913 beer was distributed through a licensing system under which the brewery would set up a saloon or acquire the license to a saloon. These saloons, termed "captive saloons," would then dis-

pense only the beer of the brewery holding the license. In 1913 Seattle, a predecessor of petitioner, owned 21 saloons and licensed considerably more. During the five-year period ended June 30, 1913, Seattle's investment in the 21 captive saloons averaged $79,347.28. Such investments were included in plant properties, in financial statements, or balance sheets.

In 1909 the State of Washington passed a local option law which provided for a vote on the liquor question in towns, cities, and the unincorporated portions of counties as separate units. In 1910 70 municipal [40] local option elections were held in the state, of which 35 voted dry, abolishing thereby 129 saloons. Of the 38 counties of the state, 10 voted under the rural county law during 1910, of which number 9 voted dry, abolishing thereby from the rural districts of these counties 40 saloons, the total number of saloons abolished during 1910 being 169. In 1912 129 elections were held, 84 of which resulted in dry victories, while 45 resulted in wet victories. As a result of these elections 360 saloons were abolished and 71 per cent of the area of the state was made dry. The unincorporated portions of 19 counties were without saloons, 4 counties were entirely dry, and 71 municipalities, including 15 county seats, had no license. In 1913 220 elections were held under the local option law, 140 of which resulted in dry victories, while only 80 resulted in wet victories. As a result of these elections, 572 saloons were abolished and 87 per cent

of the area of the state was made dry. In that year the unincorporated portions of 34 counties were without saloons and 6 counties were entirely dry. In 1913 most of the railroads had discontinued the sale of intoxicating liquors and the steamboat companies were rapidly following the example of the railroads. At that time the question of state prohibition was a live issue in the State of Washington. In 1912 and 1913 over 300 news articles and 33 editorials were published on the subject in 4 of the leading newspapers of the state. Articles on the subject appeared in leading magazines and in the yearbooks of the Anti-Saloon League and United States Breweries Association, which were available to persons desiring such information.

At March 1, 1913, local option was increasing in the State of Washington and there was a definite trend toward state-wide prohibition. The state went dry in the election of November 3, 1914. The vote was for prohibition 189,840, against 171,208.

During the fiscal year ended June 30, 1913, the management of Seattle, a predecessor of petitioner, authorized the expenditure of $128,000 on plant improvements. Substantial expenditures were made by other breweries about this time.

The following table shows sales of petitioner's predecessor in barrels and the net income from sales within and without the State of Washington for the fiscal years ended June 30, 1908, through June 30, 1912:

Year	Washington		Outside of Washington		Total	Total
	Barrels	Net income	Barrels	Net income	barrels	net income
1908	162,571	$293,353.00	98,232	$77,662.00	260,803	$371,015.00
1909	161,710	298,387.00	83,480	36,316.00	245,190	334,703.00
1910	172,612	303,160.00	93,523	38,083.00	266,135	341,243.00
1911	178,283	326,880.00	111,287	76,263.00	289,570	403,143.00
1912	171,902	353,603.00	137,909	111,381.00	309,811	464,984.00
Average	169,415	315,077.00	104,886	67,941.00	274,301	383,018.00

Of the total average net income for the five years ended June 30, 1912, 82.25 per cent is allocable to sales within the State of Washington and 17.75 per cent is allocable to sales in the territory outside of Washington.

The following table shows the petitioner's predecessor's tangible assets invested in the brewery business for the fiscal years from June 30, 1907, through June 30, 1912, including accounts receivable, but excluding bills receivable shown on the balance sheets as "investments":

	June 30, 1907	June 30, 1908	June 30, 1909	June 30, 1910	June 30, 1911	June 30, 1912
Current assets	$887,791.19	$903,354.68	$922,109.77	$855,690.85	$964,834.57	$1,150,692.53
Deferred charges....	16,317.23	9,925.81	14,852.32	13,596.24	18,301.97	14,854.84
Fixed assets—net..	1,687,211.68	1,835,185.10	1,844,162.75	1,855,896.37	1,905,017.46	1,954,843.94
Total	2,591,320.10	2,748,465.59	2,781,124.84	2,725,183.46	2,888,154.00	3,120,391.31
Less current liabilities	496,794.41	409,898.16	314,980.63	166,690.26	153,237.03	217,363.25
Net tangible assets	2,094,525.69	2,338,567.43	2,466,144.21	2,558,493.20	2,734,916.97	2,903,028.06

The average value of tangible assets during the five years ended June 30, 1912, was $2,519,379.74.

The bills receivable shown on the balance sheets for the same period were as follows:

	June 30, 1907	June 30, 1908	June 30, 1909	June 30, 1910	June 30, 1911	June 30, 1912
Bills receivable	$318,179.07	$292,206.10	$385,090.78	$449,371.14	$520,410.32	$ 598,353.75

In its income tax return for 1940 petitioner computed the value of its good will as of March 1, 1913, to be in excess of $1,000,000, which is used as a basis for computing profit or loss on the transaction in 1940, in which it granted to Century the perpetual and exclusive right to use the trade names "Rainier" and "Tacoma" in connection with the manufacture and sale of alcoholic malt beverages in the State of Washington and the Territory of Alaska in consideration of promissory notes aggregating $1,000,000. In computing the value of good will as of March 1, 1913, it used the average value of tangible assets during the five years ended June 30, 1912, which it determined to be $2,519,379.74 and the average net earnings for the same period, $383,018.91. In computing the value of the "trade-names and other intangibles" as of March 1, 1913, it allowed 8 per cent return on the average value of tangible assets, or $201,550.38, and excess earnings of $181,468.53, applicable to intangible assets. The amount applicable to intangibles was capitalized at 15 per cent, or $1,209,790.20, which it treated as the "estimated March 1, 1913, value of trade-names and other intangible assets which were sold by virtue of the grant of a [42] perpetual right to the use thereof to the Seattle Malting and Brewing Co. during 1940."

The fair market value, as of March 1, 1913, of the trade names "Rainier" and "Tacoma" apportionable to the State of Washington and the Territory of Alaska was $514,142.

Petitioner's predecessors filed income tax returns for the years 1918, 1919, and 1920, but claimed no deductions therein for obsolescence of good will or trade names. In July 1920 Seattle filed a claim for abatement of taxes for the year 1919, based on a claim for obsolescence of good will. In this claim it computed the value of the good will of Seattle as of March 1, 1913 (based on the average invested capital for the years 1903 to 1913, inclusive, which was capitalized at 10 per cent and an average earning for the same period of $81,336.04 which was capitalized at 15 per cent), to be $542,240.27. The Commissioner computed the good will value as of March 1, 1913, to be $406,680.20, which was arrived at by using the same figures as those used by Seattle, but changing the capitalization rate of good will from 15 per cent to 20 per cent. He then allocated the amount of $406,680.20 to the following years in the following amounts:

1918	$345,061.95
1919	59,153.48
1920	2,464.77
Total	406,680.20

Petitioner's predecessors, Seattle and Rainer, derived tax benefits from such allocation as follows:

1918	$78,983.92
1919	59,153.48
Total	138,137.40

In determining the deficiency here in question the respondent treated the $1,000,000 received by peti-

tioner in 1940 as ordinary income and included the entire amount in petitioner's gross income.

Opinion

Harron, Judge: Issue 1.—The first issue raised by the pleadings is whether $1,000,000 is notes received by petitioner in 1940, in consideration of the exclusive and perpetual right to use the trade names "Rainier" and "Tacoma" in the manufacture and sale of alcoholic malt beverages in the State of Washington and the Territory of Alaska, was ordinary income and taxable as such. The question turns on whether the sum of $1,000,000 is to be regarded as prepaid royalties, or whether it is to be regarded as an expenditure in the acquisition of a capital asset. [43]

The decision of this issue is governed by the decision in Seattle Brewing & Malting Co., 6 T. C. No. 856. In that case the issue was whether the taxpayer (the purchaser) was entitled to deduct from its income any portion of the $1,000,000 which on July 1, 1940, it agreed to pay to Rainier upon the exercise of the option of electing to terminate all royalties payable under the contract of April 23, 1935, under a theory that the $1,000,000 constituted a payment of royalties. The contract there under consideration was the same contract which we have before us here, and the decision of the question depended upon whether the $1,000,000 was paid in the acquisition of a capital asset or whether it was royalties paid under a licensing agreement. The evidence in the instant case is not materially different

from the evidence presented in the Seattle case. In that case we said:

> * * * We find no ambiguity in the contract and the language in paragraph thirteenth is clear. It provides that at any time after five years petitioner "shall have the right and option of electing to terminate all royalties thereafter payable hereunder" by executing and delivering to Rainier its promissory notes in the principal sum of $1,000,000. Obviously, it was intended that after the execution of the notes all royalty payments as such should cease. The agreement admits of no other construction. Thereafter Rainier must look for payment to the promissory notes and not to the contract. The execution and delivery of the notes put an end to the payment of royalties on a barrelage basis and was the consideration for the exclusive and perpetual use of such rights thereafter. It is our opinion that upon the exercise of the option petitioner acquired a capital asset for which it paid $1,000,000. * * *

Upon the authority of Seattle Brewing & Malting Co., supra, we hold that the transaction here in question was a capital transaction and the sum received by petitioner for the exclusive and perpetual right to use the trade names in the manufocture and sale of alcoholic malt beverages within the limited territory was not ordinary income within the purview of section 22 of the Internal Revenue Code.

Issue 2.—Since the sum which petitioner received

from Century on July 1, 1940, did not constitute ordinary income, but represented a payment for a capital asset, a question arises whether or not petitioner realized any gain from the transaction as it was carried out by Century. It is the contention of the petitioner that the entire face amount of the notes received in 1940 upon the exercise of the option constitutes proceeds from a sale, and that it is entitled to use as its basis, for the computation of gain or loss on the transaction, the March 1, 1913, value of the trade names, and that such value was in excess of the $1,000,000 received. Petitioner concedes, however, that in computing the adjusted basis for such property there should be deducted the sum of $138,137.40, which is that portion of the total amount of $406,680.20 "allowed" by respondent as a deduction for obsolescence of [44] good will to petitioner's predecessor in the years 1918 to 1920, inclusive, which represented a tax benefit to petitioner's predecessor.

The respondent, on the other hand, contends that petitioner is not entitled to use the March 1, 1913, value, if any, as the basis for the trade names and good will, since such property was wholly destroyed by the advent of national prohibition in 1920, and since petitioner has not shown any cost allocable to trade names incurred since that date, the new basis for the revived trade names must be considered to be zero. He further challenges the value of the trade names contended for by the petitioner and, in the alternative, contends that the agreement not to compete can not be regarded as part of the trade

names or good will transferred; that at least one-half of the $1,000,000 in option notes constituted compensation to petitioner for its agreement not to compete in the beer business in the Washington area, and was, therefore, ordinary income to petitioner; and that, accordingly, the amount received as proceeds from the sale can not be in excess of $500,000. He further contends, in the alternative, that there must be deducted from the March 1, 1913, value, in order to find an adjusted basis, the entire sum of $406,680.20 which was "allowed" as obsolescence of petitioner's predecessor for the years 1918 to 1920, inclusive.

The respondent's contention that petitioner is not entitled to use the March 1, 1913, value, if any, as the basis for the trade names and good will disposed of in 1940, because such property was wholly destroyed by the advent of national prohibition, does not find support in the record. There is no evidence whatever in the record that the trade name "Rainier" became worthless as a result of prohibition. Indeed the record conclusively establishes the contrary. The trade name was never abandoned during prohibition, but was used in the sale of near beer and soft drinks under such labels as "Rainier," "Rainier Lager," "Rainier Old German Lager," and "Rainier Malt Tonic" throughout the period of state prohibition in Washington and national prohibition thereafter. Moreover, the registration of its trade names in the United States Patent Office and in the State of Washington was kept alive from 1898 down to the present time, having been renewed

from time to time during this period. Upon the repeal of prohibition after 1932 "Rainier" beer was again put on the market by petitioner. Although it is obvious that the value attaching to the trade name "Rainier" and the good will of petitioner's predecessor corporations fluctuated very materially during the period from 1915 to 1933, it nevertheless does not follow that Rainier lost the use of its 1913 basis. The good will survived and it is immaterial that its value revived after prohibition. It has never been supposed that the fluctuation of value of property would destroy the taxpayer's basis. In fact, if a deduction has been taken for worthlessness, such deduction will [45] deprive a taxpayer of its basis only to the extent, that it results in a tax benefit. Cf. Estate of James N. Collins, 46 B. T. A. 765; affd., 320 U. S. 489, and John V. Dobson, 46 B. T. A. 770; affd., 320 U. S. 489. We are of the opinion that the petitioner's basis for determining gain or loss upon the sale of its trade names and good will in 1940 is the fair market value of such property as of March 1, 1913, adjusted under section 113 (b) (1) (B) of the Internal Revenue Code.

In the instant case it is apparent that the good will value to be applied against the amount received for the trade names in 1940 is the value of the trade names as of March 1, 1913, so the value to be placed thereon is what a willing buyer, with a full knowledge of the facts, would pay and a willing seller, not acting under any compulsion to sell, would accept for such property. In the computations by the petitioner's expert witnesses there has been no al-

lowance for the value of good will, as such, separate and apart from the trade names used in the business. The petitioner insists that the good will, as mathematically computed under an approved formula, represents the value of the trade names. Good will is an intangible, and just what goes into the caldron to make up the sum of its ingredients is sometimes difficult to determine, but it would seem clear that the value of the trade names was not the full content of good will value attached to the business of petitioner's predecessors as of March 1, 1913. In determining the value of the trade names, we have taken into consideration all of the evidence in the record, including the stipulations of the parties, the opinions of the expert witnesses, and the methods used by them in arriving at their estimated values of the good will as of March 1, 1913. We have also considered the fact that the total value of good will included other elements besides the value of the trade names, and that there was a pronounced trend toward prohibition in the State of Washington, where 82 per cent of the income from sales of petitioner's products was realized. Moreover, we have assumed a buyer conversant with all these facts. In our judgment the value of the trade names here in question as of March 1, 1913, was $514,142, and we have so found as a fact.

In C. C. Wyman & Co., 8 B. T. A. 408, we said that good will is not necessarily confined to a name. It may as well attach to a particular location where the business is transacted, or to a list of customers, or to other elements of value in the business as a going

concern. In Ithaca Trust Co. v. United States, 279 U. S. 151, Justice Holmes said that the value of the thing to be taxed must be estimated as of the time when the act is done, "but the value of property at a given time depends upon the relative intensity of the social desire for it at that time, expressed in the money that it would bring in the market." Obviously "relative intensity of the social desire" for the trade names "Rainier" [46] and "Tacoma" at March 1, 1913, would have been tempered by all of the hazards incident to the business and the future prospects of gain then apparent from the use of such trade names.

Issue 3.—The above holdings brings us to the third question, relating to the adjusted basis to be used for determining gain or loss from the transaction in 1940 wherein the petitioner granted and the purchaser, Century, acquired an exclusive and perpetual right to use the trade names "Rainier" and "Tacoma" in the manufacture and sale of alcoholic malt beverages in the State of Washington and the Territory of Alaska for $1,000,000. The applicable provision of the statute is set out in the margin.[1]

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[1]Sec. 113 (I. R. C.). Adjusted Basis for Determining Gain or Loss.

(a) Basis (Unadjusted) of Property.—The basis of property shall be the cost of such property; except that—

* * * * * * *

(14) Property Acquired Before March 1, 1913.—In the case of property acquired before March 1, 1913, if the basis otherwise determined under this subsection, adjusted (for the period prior to March

It appears from the record that petitioner's predecessors filed income tax returns for the years 1918, 1919, and 1920, but claimed no deduction therein for obsolescence of good will or trade names. In July 1920 Seattle, a predecessor, filed a claim for abatement of taxes for the year 1919 based on a claim for obsolescence of good will due to prohibition legislation. The Commissioner computed the good will value as of March 1, 1913, to be $406,680.20. Of this amount $345,061.95 was allocated to the year 1918, $59,153.48 to the year 1919, and $2,464.77 to the year 1920. It is stipulated that petitioner's predecessors derived tax benefits from such allocation in the amounts of $78,983.92 for the year 1918 and $59,153.48 for the year 1919, making a total of $138,137.40. The respondent now argues that $406,680.20 was "allowed" for obsolescence of good will and that this amount must be deducted from the March 1,

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1, 1913) as provided in subsection (b), is less than the fair market value of the property as of March 1, 1913, then the basis for determining gain shall be such fair market value. * * *

(b) Adjusted Basis.—The adjusted basis for determining the gain or loss from the sale or other disposition of property, whenever acquired, shall be the basis determined under subsection (a), adjusted as hereinafter provided.

(1) General Rule.—Proper adjustment in respect of the property shall in all cases be made—

* * * * * * *

(B) in respect of any period since February 28, 1913, for exhaustion, wear and tear, obsolescence * * * to the extent allowed (but not less than the amount allowable) under this chapter or prior income tax laws. * * *

1913, value as determined here in computing the adjusted basis under section 113 (b) (1) (B) of the Internal Revenue Code. The respondent relies on Virginian Hotel Corporation of Lynchburg v. Helvering, 319 U. S. 523; rehearing denied, 320 U. S. 810, and Commissioner v. Kennedy Laundry Co., 133 Fed. (2d) 660; certiorari denied, 319 U. S. 770; rehearing denied, 320 U. S. 810. It is the petitioner's position that because no claim was made by its predecessors for obsolescence for the years 1918 and 1920 the amount allocated to those years by the Commissioner, as to which no tax benefit was realized, has not been "allowed" within the meaning of section 113 (b) (1) (B) or within the decision of the Supreme Court in the Virginian Hotel case. It argues that no amount was "allowable" for obsolescence of good will due to prohibition within the decision of the Supreme Court in Clarke v. Haberle Crystal Springs Brewing Co., 280 U. S. 384, and, therefore, the amount of obsolescence "allowed" must be limited to the amount as to which a tax benefit was realized.

The Virginian Hotel case, supra, dealt solely with tangible assets. It is apparent from a perusal of the decision and the dissents thereto that the purpose of the statute was to limit depreciation to the taxable year in which it occurred and not permit the taxpayer to accumulate and apply it in a subsequent year when it would better suit his purpose. The Court pointed out that the provision in the statute makes it plain that the depreciation basis is reduced by the amount allowable each year,

whether or not claimed, and that the basis must be reduced by that amount even though no tax benefit results from the use of depreciation as a deduction. "Wear and tear do not wait on net income." This situation can only arise in cases dealing with depreciable property. In the opinion the Court said:

> * * * "Allowed" connotes a grant. Under our federal tax system there is no machinery for formal allowances of deductions from gross income. Deductions stand if the Commissioner takes no steps to challenge them. Income tax returns entail numerous deductions. If the deductions are not challenged, they certainly are "allowed" since tax liability is then determined on the basis of the returns. Apart from contested cases, that is indeed the only way in which deductions are allowed."

Annual depreciation in the case of good will is not permissible, because from the very nature of the asset is not depreciable. Annual depreciation can only arise in cases dealing with depreciable property. Where, as in the case here, we have non-depreciable property the same situation does not obtain. A trade name is built up over the years and in the normal course of events is appreciated rather than depreciated, so that there is no amount allowable for exhaustion during a taxable year unless during that year there is a destruction of such intangible property. The Virginian Hotel case, supra, is, therefore, not controlling here. It is distinguishable on its facts and the rationale of that

decision is not applicable here. The same may be said of Commissioner v. Kennedy Laundry Co., supra, also relied upon by the respondent.

A more serious objection to the respondent's claim, however, is the fact that the Supreme Court in Clarke v. Haberle Crystal Springs Brewing Co., supra, held that exhaustion or obsolescence of good will due to the prohibition amendment was not within the intendment of [48] the statute. In the opinion Mr. Justice Holmes, speaking for the Court, said:

> * * * It seems to us plain without help from Mugler v. Kansas, 123 U. S. 623, that when a business is extinguished as noxious under the Constitution the owners cannot demand compensation from the Government, or a partial compensation in the form of an abatement of taxes otherwise due. It seems to us no less plain that Congress cannot be taken to have intended such a partial compensation to be provided for by the words "exhaustion" or "obsolescence." Neither word is apt to describe termination by law as an evil of a business otherwise flourishing, and neither becomes more applicable because the death is lingering rather than instantaneous.

It is well settled that, when the Supreme Court declares an act of the legislature to be unconstitutional, such an act never was law and was never binding as law. By the same token, where the Supreme Court has declared that the words "exhaustion" and "obsolescence" as used in the reve-

nue laws do not include a loss of good will due to the prohibition amendment, the interpretation of the revenue laws must be to the effect that such a deduction was never granted by Congress. Since such deduction was never allowable under the revenue laws, it is difficult to see how the Commissioner by "allowing" a deduction which was never claimed can bind the taxpayer by such deduction as "allowed" within the meaning of the revenue act. In other words, a deduction "allowed," but not claimed or actually taken, can hardly be said to be "allowed" where there was no basis in the statute for such an allowance. Certainly, exhaustion and obsolescence can not be said to be allowed in the sense that those terms are used and understood by the Supreme Court in the Virginian Hotel case, supra, when applied to non-depreciable intangible assets. See also Renziehausen v. Lucas, 280 U. S. 387. We hold, therefore, that, for the purpose of computing the adjusted basis, the fair market value of the trade names as of March 1, 1913, can only be reduced by such amounts as petitioner's predecessors received tax benefits therefrom, the amount of $138,137.40.

Issue 4.—The fourth and last question is whether any part of the $1,000,000 received by petitioner in 1940 should be allocated to petitioner's agreement not to compete which is set out in paragraph ninth of the contract of April 23, 1935. The petitioner contends that such agreement was incidental to the grant by it of an exclusive and perpetual right to use the trade names, and that the agreement had no value separate and apart from the

trade names or good will. The respondent contends that at least $500,000 of the $1,000,000 paid on the exercise of the option agreement must be considered as an amount paid for the agreement not to compete.

In determining the deficiency, the respondent treated the $1,000,000 which petitioner received in 1940 as ordinary income under the royalty [49] contract, and neither in the deficiency notice[2] nor in the pleadings[3] is any value assigned by the respond-

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[2] "(a) In the taxable year you received a payment of $1,000,000.00 from the Century Brewing Association under a contract executed in 1935 whereby you granted to Century Brewing Company a license to use trade names, held by you, in connection with the marketing of beer, ale, and other alcoholic liquors made from malt, in the State of Washington and the Territory of Alaska. No income from such payment was reported in your return for 1940. You contend that the receipt of $1,000,000.00 represented the proceeds of a sale by you of good will and an interest in the trade names; that such good will and trade names have a basis, represented by the market value at March 1, 1913, in excess of the proceeds; that hence no deductible loss was allowable and no taxable gain was reportable. It is held that the contract executed in 1935 did not effect a sale of trade names or good will; that the payment of $1,000,000.00 received by you in 1940 was ordinary income taxable in full without any offset for the claimed basis.

It is further held that since the transaction did not constitute a sale, the income realized in 1940 may not be excluded from excess profits net income under section 721 of the Internal Revenue Code."

[3] Paragraph 5 (k) of the petition alleges:

"During the year 1940 Century exercised the option granted to it by said contract and delivered

ent to the agreement not to compete, and no mention is made of it. Without any question, it is well settled that any amount received for an agreement not to compete would be taxable as ordinary income. Estate of Mildred K. Hyde, 42 B. T. A. 738; John D. Beals, 31 B. T. A. 966; affd., 82 Fed. (2d) 268; Christensen Machine Co., 18 B. T. A. 256; Christensen Machine Co. v. United States (Ct. Cls.), 50 Fed. (2d) 282. There is, however, no direct evidence in the record as to the value of the agreement not to compete, nor does it appear that Century would not have purchased the exclusive right to the trade names without the agreement not to compete. Certainly there is nothing in the record to indicate that such agreement not to compete was worth $500,000.

It is obvious that in 1935, when the contract between petitioner and Century was entered into, an agreement not to compete had a substantial value, and it can not be said that paragraph ninth of the contract was mere words. It was perfectly possible for petitioner to sell the exclusive and perpetual right to use its trade names in the limited territory without any agreement not to compete, and it is conceivable that in that situation it might have

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to petitioner promissory notes in the principal amount of $1,000,000.00, as a lump sum payment for the exclusive and perpetual right and license thereafter to manufacture and market beer, ale and other alcoholic malt beverages within the State of Washington and the Territory of Alaska under the trade names and brands of 'Rainier' and 'Tacoma'." This allegation was admitted by the respondent in his answer.

continued selling beer in the territory under another trade name. Undoubtedly such competition, backed by petitioner's advertising and sales organization and by the good will attached to its corporate name, would have had some effect upon the sale of beer by Century under the trade name "Rainier." Moreover, there was obviously a nuisance value attaching to the right to compete which the purchaser of the trade name would want to eliminate, but any competition would be seriously narrowed by the equity rule, which [50] was followed in the State of Washington, that the sale of the good will of a business carries with it an implied covenant by the seller that he will not solicit the custom for which the purchaser paid, and with which he parted, for the consideration received. So, while the petitioner, in the absence of an agreement not to compete, might have been at liberty to engage in a similar business in the same locality in his own name, it is very doubtful whether he could have sold the same beer under another name and advertised the fact without being enjoined by the purchaser of his trade names. In Cooper & Co. v. Anchor Securities Co. (Supreme Court of Washington, 1941), 113 Pac. (2d) 845, suit was brought to restrain Anchor Securities Co. and its officers from directly soliciting insurance business from defendant's former customers after a sale of the business and good will to the plaintiff. In its opinion, holding that an injunction should issue, the court said:

> In the absence of express or implied conditions in the contract of sale of a business to-

> gether with the good will thereof to the contrary the vendor is at liberty to set up a similar business in the same locality and carry it on in his own name. Annotations 11 Ann. Cas. 573 et seq; 19 L. R. A., N. S., 762 et seq; 82 A. L. R. 1030 et seq. However, the sale of good will of a business carries with it, even in the absence of a restrictive covenant, the implied obligation that the seller will not solicit his old customers or do any act that would interfere with the vendee's use and enjoyment of that which he had purchased.

Upon the advent of prohibition in Washington petitioner built a brewery in California and thereafter manufactured beer in that state. Having resumed the sale of beer in the State of Washington after the repeal of prohibition in 1933, it had undoubtedly built up an advertising and sales organization for that state. When the contract of April 23, 1935, was entered into it owned the old brewery property at Seattle, which it used for offices and as a cold storage plant and warehouse. But under the contract the old brewery property was sold to Century and petitioner discontinued its beer business in the State of Washington. This situation continued during the five-year period from 1935 to 1940, during which time its transactions with Century were on a royalty basis, so that in 1940, when petitioner sold the exclusive and perpetual right to use its trade names and brands in connection with the manufacture and sale of alcoholic malt beverages, it was not engaged in any business of selling

alcoholic malt beverages in the State of Washington. During this five-year period, from 1935 to 1940, Century had built up its sales of "Rainier" beer through advertising and its own sales organization from 60,000 barrels sold in 1936 to 131,000 barrels sold in 1940, so that the agreement by petitioner not to compete had little, if any, value in 1940. In the opinion of the Board of Tax Appeals in Christensen Machine Co., supra, it was said, in discussing an agreement not to compete for a period of five years: [51]

> * * * It (the purchaser) thus obtained the right to conduct its business free from Christensen's competition during a period when it was not in a strong position. This was a valuable asset in the hands of the petitioner, the benefits of which would continue over a period which would not necessarily be coextensive with the five-year period provided in the agreement. To illustrate, the petitioner in two years' time might have so strengthened its position that Christensen's competition could not affect it, or in the five years it might have so strengthened its position that as a consequence for one or more years thereafter Christensen's competition would be less severe than it otherwise would have been. The fact remains, however, that as each year passed, the time was that much nearer when the benefits derived from the contract would be completely exhausted. (Emphasis supplied.)

It must be borne in mind that the sale here in question was made in 1940 and not in 1935. In our judgment, considering all of the facts and the legal restrictions under which petitioner would have had to compete had it chosen to do so, we are of the opinion that any value which the agreement not to compete had in 1935 had been exhausted when, in 1940, Century elected to exercise the option and purchase the exclusive and perpetual right to use the trade names in its business.

We hold, therefore, that no part of the $1,000,000 received by petitioner for the exclusive and perpetual right to use its trade names in the State of Washington and the Territory of Alaska was received in payment for its agreement not to compete with the purchaser in that territory.

Decision will be entered under Rule 50. [52]

[Title of Tax Court and Cause.]

DECISION

Pursuant to the Findings of Fact and Opinion in this proceeding which were promulgated on June 18, 1946, respondent filed a recomputation under Rule 50, in which petitioner acquiesces. Accordingly, it is

Ordered and Decided: That for the year 1940 there is a deficiency in income tax in the amount of $149,548.89; that there are no deficiencies in de-

clared value excess profits tax and excess profits tax; and that for the year 1941 there is a deficiency in excess profits tax in the amount of $15,338.15.

[Seal] /s/ MARION J. HARRON,
Judge.

Entered Aug. 12, 1946. [53]

In the United States Circuit Court of Appeals
for the Ninth Circuit

T. C. No. 4895

COMMISSIONER OF INTERNAL REVENUE
Petitioner on Review,

vs.

RAINIER BREWING COMPANY,
Respondent on Review.

PETITION FOR REVIEW

To the Honorable Judges of the United States Circuit Court of Appeals for the Ninth Circuit:

Now Comes the Commissioner of Internal Revenue, by his attorneys, Sewall Key, Acting Assistant Attorney General; J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, and Charles E. Lowery, Special Attorney, Bureau of Internal Revenue, and respectfully shows:

I.

That this proceeding is concerned with a redetermination of Federal income, declared value excess

profits, and excess profits tax liability of the respondent, Rainier Brewing Company (sometimes hereinafter referred to as the taxpayer), for the taxable year 1940 and excess profits tax liability for the year 1941. The taxpayer's income and excess profits tax returns for the taxable years 1940 and 1941 were filed with the Collector of Internal Revenue for the First California District whose office is located in the City of San Francisco, California, and within the jurisdiction of the United States Circuit Court of Appeals for the Ninth Circuit. [54]

II.

The nature of the controversy is as follows, to wit:

The taxpayer is a corporation organized under the laws of the State of California with its principal office and place of business in the City and County of San Francisco, California. Prior to the advent of prohibition a company by the name of Seattle Brewing & Malting Company had sold beer in the Seattle area under the name "Rainier." The taxpayer is the successor of the latter company. The value of the name "Rainier" having been developed through extensive prior use, a competitor of the taxpayer known as the Century Brewing Association approached officers of the taxpayer during the year 1935, following the repeal of prohibition, with a view to acquiring from the taxpayer the right to use the trade name "Rainier" and "Tacoma" in the manufacture and sale of beer and alcoholic beverages in the State of Washington and the territory of Alaska and to have the name Seattle Brewing &

Malting Company. A contract was entered into between the taxpayer and the Century Brewing Association on April 23, 1935. This contract sold certain plant, equipment and facilities, and in addition licensed to the Century Brewing Association the "sole and exclusive perpetual right and privilege" of manufacturing and marketing beer and other alcoholic malt beverages under the name "Rainier" within Washington and Alaska. Payment for the right to use the trade name was to be on a barrelage royalty basis, with a provision that at its option after five years Century could terminate all future royalties on a barrelage basis by executing promissory notes payable over a period of five years and totaling $1,000,000. The contract also provided that the taxpayer would not compete within the stated territory; that it would maintain the trade name registration; that Century would maintain quality of product equal to that of the taxpayer; that Century would expend sums advertising [55] "Rainier" at least equal to that of other brands; and that it would not assign any rights under the contract without the consent of the taxpayer. In 1940 Century elected to terminate payment on the barrelage royalty basis and executed five non-negotiable notes of $200,000 each, due successively in each of five years. The notes were later paid before maturity in consideration of the grant of the use of the name of "Rainier" in Idaho and because of other considerations.

III.

In its income tax return for the year 1940 the taxpayer computed the value of its good will as of March 1, 1913, to be in excess of $1,000,000 which value was used by it as a basis for computing profit or loss on the transaction in 1940 in which it granted to Century the perpetual and exclusive right to use the trade names "Rainier" and "Tacoma" in connection with the manufacture of beer and alcoholic beverages in the State of Washington and the Territory of Alaska in consideration of Century's promissory notes aggregating $1,000,000. In his deficiency determination the Commissioner treated the $1,000,000 received by the taxpayer in 1940 as ordinary income, rather than the proceeds from the sale of a capital asset, and accordingly included the entire amount in the taxpayer's gross income. It was further held by the Commissioner that since the transaction did not constitute a sale, the income received in 1940 could not be excluded from excess profits net income under Section 721 of the Internal Revenue Code. The Tax Court of the United States held that the amount received by the taxpayer in 1940 constituted proceeds from the sale of a capital asset andwas not, therefore, ordinary income. The Tax Court also [56] held that the taxpayer's basis for determining gain or loss on the sale of its trade names and good will in 1940 was the fair market value of such property as of March 1, 1913, adjusted under Section 113(b)(1)(B) of the Internal Revenue Code, the fair market value so determined being $514,142 less the amount of $138,137.40, a por-

tion of a total amount of $406,680.20 which the Commissioner had previously allowed as a deduction for obsolescence of good will to the taxpayer's predecessors in the years 1918, 1919 and 1920, the smaller amount of $138,137.40 representing a tax benefit received by the taxpayer's predecessors for the years 1918 and 1919 from such allowance. The Tax Court's findings of fact and opinion was promulgated on June 18, 1946, and its decision pursuant to such opinion was entered on August 12, 1946, "that for the year 1940 there is a deficiency in income tax in the amount of $149,548.89; that there are no deficiencies in declared value excess profits tax and excess profits tax; and that for the year 1941 there is a deficiency in excess profits tax in the amount of $15,338.15."

IV.

The petitioner being aggrieved by the Tax Court's findings of fact and opinion dated June 18, 1946, and by its decision entered on August 12, 1946, desires to obtain a review thereof before the United States Circuit Court of Appeals for the Ninth Circuit in accordance with the provisions of Sections 1141 and 1142 of the Internal Revenue Code. [57]

Wherefore, he petitions that a transcript of the record be prepared in accordance with the rules of the United States Circuit Court of Appeals for the Ninth Circuit and transmitted to the Clerk of said Court for filing and appropriate action, to the end that the errors complained of may be reviewed

and corrected by the said United States Circuit Court of Appeals for the Ninth Circuit.

/s/ SEWALL KEY, CAR
Acting Assistant Attorney General.

/s/ J. P. WENCHEL CAR
Chief Counsel, Bureau of Internal Revenue,

Attorneys for Petitioner on Review.

Of Counsel:
CHAS. E. LOWERY,
Special Attorney,
Bureau of Internal Revenue.

Received and Filed T.C.U.S. Nov. 5, 1946. [58]

[Title of Circuit Court of Appeals and Cause.]

NOTICE OF FILING PETITION FOR REVIEW

To: A. Calder Mackay, Esquire,
728 Pacific Mutual Building,
Los Angeles 14, California.

You are hereby notified that the Commissioner of Internal Revenue did, on the 5th day of November, 1946, file with the Clerk of The Tax Court of the United States, at Washington, D. C., a petition for review by the United States Circuit Court of Appeals for the Ninth Circuit of the decision of

The Tax Court heretofore rendered in the above-entitled cause. A copy of the petition for review as filed is hereto attached and served upon you.

Dated this 5th day of November, 1946.

/s/ J. P. WENCHEL CAR
Chief Counsel, Bureau of Internal Revenue,
Counsel for Petitioner on Review.

Personal service of the above and foregoing notice, together with a copy of the petition for review, is hereby acknowledged this 8th day of November, 1946.

/s/ A. CALDER MACKAY,
Attorney for Respondent on Review.

Received and Filed T.C.U.S. Nov. 14, 1946. [59]

[Title of Circuit Court of Appeals and Cause.]

NOTICE OF FILING PETITION FOR REVIEW

To: Rainier Brewing Company,
1550 Bryant Street,
San Francisco, California.

You are hereby notified that the Commissioner of Internal Revenue did, on the 5th day of November, 1946, file with the Clerk of The Tax Court of the United States, at Washington, D. C., a petition for review by the United States Circuit Court

of Appeals for the Ninth Circuit of the decision of the Tax Court heretofore rendered in the above-entitled cause. A copy of the petition for review as filed is hereto attached and served upon you.

Dated this 5th day of November, 1946.

/s/ J. P. WENCHEL CAR
Chief Counsel, Bureau of Internal Revenue,
Counsel for Petitioner on Review.

Personal service of the above and foregoing notice, together with a copy of the petition for review, is hereby acknowledged this 12th day of November, 1946.

RAINIER BREWING COMPANY.

By /s/ F. S. SMITH,
Secretary,
Respondent on Review.

Received and Filed T.C.U.S. Nov. 18, 1946. [60]

The Tax Court of the United States

Docket No. 4895

RAINIER BREWING COMPANY,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

STIPULATION

It is hereby stipulated and agreed by and between the parties hereto, through their respective counsel, that—

I.

The re-organization referred to in Paragraph V (e) of the Petition and Answer herein was a non-taxable re-organization within the meaning of the applicable provisions of the Internal Revenue Laws, whereby Seattle Brewing and Malting Co. (the West Virginia corporation) and its wholly-owned subsidiary, Rainier Brewing Company (the Washington corporation), made the transfers to Pacific Products, Inc. referred to in Paragraph V (e) of the Petition, without the recognition of any gain or loss, in exchange solely for the stock or securities of Pacific Products, Inc., and immediately after the transfer an interest or control in such assets of 50 per centum or more remained in the same persons. Attached hereto, marked Exhibits "A" and "B," and made a [61] part hereof, are true and complete cop-

ies of the assignments by which said transfers were effected.

II.

In the year 1932 Pacific Products, Inc. transferred to Rainier Brewing Company, Inc. (a California corporation organized in 1932), its assets of every kind and description, save and except certain designated assets not used in the conduct of its manufacturing business. Attached hereto, marked Exhibits "C" and "D," and made a part hereof, are true and complete copies of the "General Transfer (other than real estate)" and the Grant Deed by which said transfer was effected. Said transaction was a nontaxable re-organization within the meaning of the applicable provisions of the Internal Revenue Laws whereby said property, without the recognition of any gain or loss, was transferred to Rainier Brewing Company, Inc. in exchange solely for the stock or securities of Rainier Brewing Company, Inc., and immediately after the transfer an interest or control in such property of 50 per centum or more remained in the same persons.

III.

The statutory merger or consolidation referred to in Paragraph V (h) of the Petition and Answer was a merger of Rainier Brewing Company, Inc. and Pacific Products, Inc., dated November 1, 1937, whereby Rainier Brewing Company, Inc. was merged into Pacific Products, Inc. and its separate existence ceased; and Pacific Products, Inc. became the surviving corporation, changing its name [62] to Rainier Brewing Company. Said transaction con-

stituted a non-taxable re-organization within the meaning of the applicable provisions of the Internal Revenue Laws, wherein no gain or loss was recognized.

/s/ A. CALDER MACKAY,
ADAM Y. BENNION,
Counsel for Petitioner.

Of Counsel:

/s/ F. SANFORD SMITH,
CLIFFORD J. MacMILLAN,
O. J. SONNENBERG,
SCOTT H. DUNHAM,
/s/ J. P. WENCHEL DHN
Chief Counsel, Bureau of Internal Revenue,
Counsel for Respondent.

EXHIBIT "A"

This Indenture, made and entered into as of the first day of October, 1925, by and between Seattle Brewing & Malting Company, a corporation organized and existing under and by virtue of the laws of West Virginia, having its principal place of business in the City and County of San Francisco, State of California, party of the first part, and Pacific Products, Inc., a corporation organized and existing under and by virtue of the laws of the State of California, party of the second part,

Witnesseth:

In consideration of the sum of Ten Dollars ($10.00), lawful money of the United States of America, and of other good and valuable consid-

eration, receipt whereof is hereby acknowledged, the party of the first part hereby assigns, sets over and transfers unto the party of the second part, its successors and assigns, the whole of its assets of every character and description whatsoever, including its goodwill, trade name, trade mark, trade label, copyrights, and the full benefit thereof; also all of its right, title and interest in and to all real and personal property of whatsoever character and wheresoever situated.

The party of the second part hereby accepts the foregoing assignment and in consideration thereof assumes all the liabilities of the party of the first part, as shown by its books of account on the 30th day of September, 1925, not exceeding in the aggregate the sum of Twenty-nine Thousand Seven Hundred Seventy-six and 37/100 Dollars ($29,776.37)

In Witness Whereof, the parties hereto have caused these presents to be executed in their corporate names and under their corporate seals, by their officers thereunto [64] duly authorized, the day and year first hereinabove written.

SEATTLE BREWING & MALTING COMPANY,
By /s/ LOUIS HEMRICH,
President.
F. J. McCARTHY,
Secretary.

[Seal] PACIFIC PRODUCTS, INC.
By /s/ JOSEPH GOLDIE,
Vice-President.
F. S. SMITH,
Asst. Secretary. [65]

State of California,
City and County of San Francisco—ss.

On this 15th day of June, in the year one thousand nine hundred and twenty-six, before me, George D. Perry, a Court Commissioner of the City and County of San Francisco, State of California, residing therein, duly commissioned and sworn, personally appeared Joseph Goldie and F. S. Smith, known to me to be the Vice President and Assistant Secretary, respectively, of Pacific Products, Inc., the corporation that executed the within instrument, and known to me to be the persons who executed the within instrument on behalf of the corporation therein named, and acknowledged to me that such corporation executed the same.

In Witness Whereof, I have hereunto set my hand and affixed Official Seal, at my office in the City and County of San Francisco, day and year in this Certificate first above written.

(Seal) GEORGE D. PERRY,
Court Commissioner of the City and County of San Francisco, State of California.

State of California,
City and County of San Francisco—ss.

On this 15th day of June, in the year one thousand nine hundred and twenty-six, before me, George D. Perry, a Court Commissioner of the City and County of San Francisco, State of California, residing therein, duly commissioned and sworn, personally appeared Louis Hemrich and F. J. Mc-

Carthy, known to me to be the President and Secretary, respectively of Seattle Brewing & Malting Company, the corporation that executed the within instrument, and known to me to be the persons who executed the within instrument on behalf of the corporation therein named, and acknowledged to me that such corporation executed the same.

In Witness Whereof, I have hereunto set my hand and affixed my Official Seal, at my office in the City and County of San Francisco, the day and year in this Certificate first above written.

(Seal) GEORGE D. PERRY,
Court Commissioner of the City and County of San Francisco, State of California. [66]

Dated October 1, 1945.

EXHIBIT "B"

This Indenture, made and entered into as of the first day of October, 1925, by and between Rainier Brewing Company, a corporation organized and existing under and by virtue of the laws of the State of Washington, party of the first part, and Pacific Products, Inc., a corporation organized and existing under and by virtue of the laws of the State of California, party of the second part,

Witnesseth:

In consideration of the sum of Ten Dollars ($10.00), lawful money of the United States of America, and of other good and valuable consideration, receipt whereof is hereby acknowledged, the party of the first part hereby assigns, sets over and transfers unto the party of the second part, its

successors and assigns, the whole of its assets of every character and description whatsoever, including its goodwill, trade name, trade mark, trade label, copyrights, and the full benefit thereof; also all of its right, title and interest in and to all real and personal property of whatsoever character and wheresoever situated.

The party of the second part hereby accepts the foregoing assignment and in consideration thereof, assumes all the liabilities of the party of the first part, as shown by its books of account on the 30th day of September, 1925, not exceeding in the aggregate the sum of Two Hundred Thousand Sixty and 46/100 Dollars ($200,060.46).

In Witness Whereof, the parties hereto have caused these presents to be executed in their corporate names and under their corporate seals, by their officers thereunto [68] duly authorized, the day and year first hereinabove written.

RAINIER BREWING COMPANY,

[Seal] /s/ By LOUIS HEMRICH,
President.

/s/ F. J. McCARTHY,
Secretary.

PACIFIC PRODUCTS, INC.,

By /s/ JOSEPH GOLDIE,
Vice-President.

/s/ F. S. SMITH,
Asst. Secretary. [69]

State of California,
City and County of San Francisco—ss.

On this 15th day of June, in the year one thousand nine hundred and twenty-six, before me, George D. Perry, a Court Commissioner of the City and County of San Francisco, State of California, residing therein, duly commissioned and sworn, personally appeared Louis Hemrich and F. J. McCarthy, known to me to be the President and Secretary, respectively, of Rainier Brewing Company, the corporation that executed the within instrument, and known to me to be the persons who executed the within instrument on behalf of the corporation therein named, and acknowledged to me that such corporation executed the same.

In Witness Whereof, I have hereunto set my hand and affixed my Official Seal, at my office, in the City and County of San Francisco, the day and year in this Certificate first above written.

[Seal] GEORGE D. PERRY,

Court Commissioner of the City and County of San Francisco, State of California.

State of California,
City and County of San Francisco—ss.

On this 15th day of June, in the year one thousand nine hundred and twenty-six, before me, George D. Perry, a Court Commissioner of the City and County of San Francisco, State of California, residing therein, duly commissioned and sworn, per-

sonally appeared Joseph Goldie and F. S. Smith, known to me to be the Vice President and Assistant Secretary, respectively, of Pacific Products, Inc., of the corporation that executed the within instrument, and known to me to be the persons who executed the within instrument on behalf of the corporation therein named, and acknowledged to me that such corporation executed the same.

In Witness Whereof, I have hereunto set my hand and affixed my Official Seal, at my office in the City and County of San Francisco, the day and year in this Certificate first above written.

[Seal] GEORGE D. PERRY,

Court Commissioner of the City and County of San Francisco, State of California. [70]

Dated: October 1, 1925. [71]

EXHIBIT C

General Transfer

(Other than real estate)

Pacific Products, Inc.,

to

Rainier Brewing Company, Inc.

This Indenture, dated the 11th day of October, 1932, between Pacific Products, Inc., a corporation of the State of California, (hereinafter called the Seller), party of the first part, and Rainier Brew-

ing Company, Inc., a like corporation, (hereinafter called the Buyer), party of the second part,

Witnesseth:

Whereas, the Seller is a corporation of the State of California, engaged, among other things, in the business of manufacturing and selling ale, beer, porter and other beverages and beverage products and ingredients thereof, including beverages containing what at any time may be the maximum legal alcoholic content, and of dealing in malt and hops and the products thereof, and owning and operating a brewery in the City and County of San Francisco, State of California, and owning property located in the City of Seattle, County of King, State of Washington, and having its principal office for the transaction of business in the City and County of San Francisco, State of California; and

Whereas, shareholders of the Seller holding of record at least two-thirds of the Seller's issued and outstanding shares, have consented to the sale, grant, transfer and conveyance of the Seller's business, franchises and property, real and/or personal, as a whole, save and except properties not used by the Seller in the conduct of its manufacturing business, which said properties are valued upon the Balance Sheet of the Seller prepared by Haskins & Sells, Certified Public Accountants, as of July 31, 1932, at $178,776.54 and which said properties are fully described upon Exhibit "A" hereto attached, all of which said excepted properties are herein-

after referred to and known as the "excepted properties," to the Buyer, for 50,000 Class A Common shares and 400,000 Class B Common shares of the Buyer to be issued to the Seller in the manner hereinafter provided, and the assumption by the Buyer of, and its undertaking to pay, satisfy and discharge as and when the same become payable, all debts and liabilities of the Seller existing on the 31st day of July, 1932; and

Whereas, at a special meeting of the Board of Directors of the Seller duly called and held at the office of the Seller on the 11th day of October, 1932, at which meeting a majority of said Board was present and acting, a resolution was adopted authorizing and directing the President and Secretary of the Seller, for and on its behalf and in its corporate name, to sign, seal, acknowledge and deliver to the Buyer this particular Instrument of Transfer upon the receipt from the Buyer of its agreement to issue said 50,000 Class A shares and 400,000 Class B shares of the Buyer, and the agreement of the Buyer assuming, undertaking and agreeing to pay, satisfy and discharge the debts, obligations and liabilities of the Seller existing on July 31, 1932; and

Whereas, the Buyer has delivered to the Seller, the agreement of the Buyer to issue to the Seller 50,000 Class A shares and 400,000 Class B shares of the Buyer, and the Buyer has also delivered to the Seller the agreement of the Buyer assuming, undertaking and agreeing to pay, satisfy and discharge the debts, obligations and liabilities of the Seller, as above provided, the receipt of which, at or be-

fore the [73] delivery of these presents, is hereby acknowledged by the Seller,

Now, Therefore, in consideration of the premises, the Seller has sold, assigned, transferred, set over, granted and conveyed and by these presents does sell, assign, transfer, set over, grant and convey unto the Buyer, and its successors and assigns, as of the 31st day of July, 1932, all of the Seller's business, franchises and property, as a whole, including, among other things, all personal property of whatever kind or nature which the Seller owns or in which it has any right, title or interest, including all machinery, tools, movable equipment, all stocks of materials on hand, book accounts, claims, demands and causes of action against others, good will, trade names, trade-marks, brands, patent and contract rights, cash in bank and in the Seller's office, and all fixtures, equipment, office furniture, trucks, automobiles, shares of stock of other corporations, and all other personal property connected with or used in connection with the Seller's business, and all other assets of whatsoever kind or nature and wheresoever situate, save and excepting the excepted properties which said properties are hereby retained by the Seller, and excepting the real property and real estate interests owned by the Seller which are the subject matter of separate indentures executed and delivered contemporaneously with the execution and delivery of this indenture, it being the true intent and purpose of this indenture to grant and transfer to the Buyer and its successors and assigns, all assets, of every

nature and description whatsoever and wheresoever situated, owned by the Seller or in which the Seller has any right, title or interest, and which are not conveyed to the Buyer by said indentures executed and delivered contemporaneously herewith, as aforesaid, save and excepting, however, the excepted properties, so that, by the execution and delivery of this indenture and said other indentures, the Buyer shall be vested with, and be the owner of, all of the business, franchises and property of the Seller, as a whole, save and except said excepted properties, as of the 31st day of July, 1932, as the Buyer's own absolute property. [74]

To Have And To Hold the said property and interests hereby sold, assigned, transferred, set over, granted and conveyed to and for the own proper use and behoof of the Buyer, its successors and assigns, forever.

This Indenture further witnesseth that, for the consideration aforesaid, the Seller hereby constitutes and appoints the Buyer, its successors and assigns, the true and lawful attorney or attorneys irrevocable of the Seller, with full power of substitution, for the Seller and in its name and stead, but on behalf of and for the benefit of the Buyer, its successors and assigns, to demand and receive from time to time any and all property, tangible and intangible, hereby sold, assigned, transferred, set over, granted and conveyed, or intended so to be, and to give receipts and releases for and in respect of the same or any part thereof, and from time to time to institute and prosecute in the name

of the Seller, or otherwise, but at the expense and for the benefit of the Buyer, its successors and assigns, any and all suits, actions or proceedings at law, in equity, or otherwise, which the Buyer, its successors or assigns, may deem proper, to collect, assert or enforce any claim, right or title of any kind hereby sold, assigned, transferred, set over, granted and conveyed, or intended so to be, and to defend or compromise any and all actions, suits or proceedings in respect of any of the property hereby sold, assigned, transferred, set over, granted and conveyed, or intended so to be, and to do all acts and things in relation to said property as the Buyer, its successors and assigns, shall deem desirable; the Seller hereby declaring that the foregoing powers are coupled with an interest in the Buyer, its successors and assigns, and are and shall be irrevocable by the Seller, or by its dissolution, or in any manner or for any reason. [75]

This Indenture Further Witnesseth that, for the considerations aforesaid, the Seller hereby for itself, its successors and assigns, covenants with the Buyer, its successors and assigns, that it will do, execute, acknowledge and deliver or will cause to be done, executed, acknowledged and delivered, all and very such further acts, deeds, transfers, assignments, conveyances, powers of attorney and assurances for the better assuring, conveying and confirming unto the Buyer, its successors and assigns, all and singular, the property hereby sold, assigned, transferred, set over, granted and conveyed, or in-

tended so to be, as the Buyer, its successors or assigns, shall reasonably require.

In Witness Whereof, the Seller has caused this indenture to be executed by its President and its Secretary, and its corporate seal to be hereunto affixed, the day and year first above written.

[Seal] PACIFIC PRODUCTS, INC.,
By LOUIS HEMRICH,
President.
By F. J. McCARTHY,
Secretary. [76]

State of California,
City and County of San Francisco—ss.

On this 11th day of October, in the year one thousand nine hundred and thirty-two, before me, James F. McCue, a Notary Public in and for said City and County and State, residing therein, duly commissioned and sworn, personally appeared Louis Hemrich and F. J. McCarthy, known to me to be the President and Secretary, respectively, of Pacific Products, Inc., the corporation that executed the within instrument, and they acknowledged to me that such corporation executed the same.

In Witness Whereof, I have hereunto set my hand and affixed my Official Seal at my office in the City and County and State aforesaid, the day and year in this Certificate first above written.

[Seal] /s/ JAMES F. McCUE,

Notary Public in and for the City and County of San Francisco, State of California. [77]

EXHIBIT "A"

Excepted Properties Referred to in Foregoing Instrument

State and County where located	Description of Property	Valuation upon July 31, 1932, Balance Sheet, Pacific Products, Inc.
State of Washington		
Snohomish	Lot 5, Block 6, (Snohomish County) Town of Machias.	
	Lot 6, Block 6, (Snohomish County) Town of Machias	$ 250.00
	(Improvements worthless)	
	Lot 5, Block 29, Plat of Arlington.	
	Lot 6, Block 29, Plat of Arlington.	
	(Building torn down)	687.06
	Sec. 4, Tp. 32, R. 6, Acres 40, the N.W. ¼ of the S.W. ¼ of, together with timber situated thereon.	
	(Timber claim)	1,181.97
	Lot 11, Sec. 12, Tp. 32, R.N. 8 E. WM. All that portion lying North of the N.P. Ry., and between said railway as now located and the North Fork of the Stillaguamish River.	
	(Bldg. sold for second hand lumber)	475.00
Skagit	Sec. 20, Tp. 35, R. 11, Acres 160, (Skagit County) The SE ¼	
	(Timber Claim)	
	Sec. 25, Tp. 34, R. 4 Tax Lot No. 3	
	(Unimproved.)	1,347.83
	Lot 9, Block 1, (Skagit County) Plat of G. Rassmere	
	Lot 10, Block 1, (Skagit County) Plat of G. Rassmere.	
	(Unimproved)	125.00

State and County where located	Description of Property	Valuation upon July 31, 1932, Balance Sheet, Pacific Products, Inc.
State of Washington		
Whatcom	Sec. 30, Tp. 40, R. 6 E. WM. Maple Falls. Com. at NE cor. of NE¼ of NE¼ of SW¼ of th. W. 33 ft. th. S. 261 ft., th. W. 90 ft., th. S. 30 ft. th. E. 90 ft. th. N. to beginning. Described as Tax Lot #15. (One story frame store building.)	144.47
State of California		
Los Angeles	1/7th Interest in Lot 18 McDonald Tract Los Angeles, California, located near suburb of El Nido	3,314.21
King	Lot 1, Block 323, Seattle Tide Lands, (Unimproved—First Ave. and Connecticut St.)	28,885.69
"	Lot 1, Block 12, Bay View Add. to Salmon Bay Lot 2, Block 12, Bay View Add. to Salmon Bay Lot 3, Block 12, Bay View Add. to Salmon Bay Lot 4, Block 12, Bay View Add. to Salmon Bay	21.33
	(Unimproved—Near Fort Lawton.)	
"	Lot 16, 21, and 25, Tracts 16, 21, and 25 Rainier Beach Garden Tracts, as per Map recorded in Vol. 9, of Plats, Page 37, Records of King County. (Improved with one story frame bldg. Matheson & Deady Property.)	12,935.09
"	Lot 4, Block 96, Seattle Tide Lands, J. G. Pierce Lot 5, Block 96, Seattle Tide Lands, J. G. Pierce Unimproved—Smith Cove, Puget Avenue.)	544.50

State and County where located	Description of Property	Valuation upon July 31, 1932, Balance Sheet, Pacific Products, Inc.
State of Washington		
King	Lot 12, Block 4, Town of Berlin, (Improved with small shack)	50.00
"	Sec. 22, Tp. 20, R. 10, Northwest quarter of southwest quarter. (Ellis property near Green River Hot Springs)	
"	Sec. 22, Tp 20, R. 10, Southwest quarter of southwest quarter. (Ellis property near Green River Hot Springs)	1,200.00
Clallam	Lot 3 and the East half of the SW. quarter (Timber claim) Lot 4, Sec. 7, Tp. 30, R. 8 W. Acres 160, (Clallam County) And the East half of the SW. quarter. (Timber claim)	1,000.00
Chelan	Lot 3, Block 4, (Chelan County) Town of Leavenworth (Improvements condemned)	6,133.42
"	Lot 9, Block 1, Ralston's Add. to Town of Leavenworth. (Unimproved)	250.00
Island	Sec. 10, Tp. 29, R. N. 3 E. Acres 40, (Island County) The NW ¼ of the SE. ¼ excepting therefrom the N. ½ of the NE. ¼ of the NW. ¼ of the SE. ¼ of Sec. 10, Tp. 29, N.R. 3 E. WM. containing 5 acres (cleared land)	2,507.00
Kitsap	Lot 12, Block 11, (Kitsap County) Town of Bremerton (Improved Brick bldg.—1 story)	7,989.79
Mason	Sec. 8, Tp. 21, R.N. 3 W., Acres 25 (Mason County) W. ½ and S. ½ of W. ½ of E. ½ of NW. ¼ of NE. ¼	500.00
King	Tract 9, (Matheson & Deady) of Sturtevant's Rainier Beach Valley Tracts to King County (small shack)	1,551.18

State and County where located	Description of Property	Valuation upon July 31, 1932, Balance Sheet, Pacific Products, Inc.
State of Washington		
King	Lot 7, Block 3, Hillman City Division 3	
	Lot 8, Block 3, Hillman City Division 3	488.88
"	Lot 13, Block 7, Kinnear's First Rainier Beach Addition	
	Lot 14, Block 7, Kinnear's First Rainier Beach Addition (unimproved)	1.00
"	Sec. 31, Tp. 26, N. 4 E., WM. 2½ acres (Caswell Green Lakes) acreage S. ½ of S. ½ of SE. ¼ of SE. ¼ of, approximately 2½ acres, excepting a strip 30 ft. wide off the E. margin for a road, and a strip 30 ft. wide off the W. margin for a road. (3 room frame bldg.)	2,300.00
"	Lot 14, Block 108, Gilman Park Addition to Seattle,	
	Lot 15, Block 108, Gilman Park Addition to Seattle,	
	Lot 16, Block 108, Gilman Park Addition to Seattle,	
	Lot 17, Block 108, Gilman Park Addition to Seattle. (Unimproved)	
	Lot 1, Block 13, Gilman Park Add. to Seattle	
	Lot 2, Block 13, Gilman Park Add. to Seattle	
	Lot 22, Block 13, Gilman Park Add. to Seattle	
	Lot 23, Block 13, Gilman Park Add. to Seattle	
	Lot 24, Block 13, Gilman Park Add. to Seattle (Improved with Brewery, Bottling Works, Stable, etc.)	12,751.08
"	Lot 5, Block 20, Anderson's Addition to Pontius (Frame garage bldg. with brick floor)	5,250.00

State and County where located	Description of Property	Valuation upon July 31, 1932, Balance Sheet, Pacific Products, Inc.
State of Washington		
King	Lot 35, Block 4, Ballard Addition to Seattle,	
	Lot 36, Block 4, Ballard Addition to Seattle	
	826 W North 63rd Street	
	(6-room frame dwelling)	2,095.48
"	Lot 19, Block 13, F. F. Day's First Addition	
	Lot 5, Block 8, F. F. Day's First Addition	
	(Unimproved)	800.00
"	Lot 11, Block 13, Hills Tract, S. 112 Feet	
	Lot 12, Block 13, Hills Tract, S. 112 Feet	
	1600-1602 Main Street (frame duplex house)	6,092.73
"	Lot 4, Block 22, First Plat of West Seattle by W. S. Land & Improvement Company (unimproved)	777.56
"	Lot 45, Block A; C. D. Hillman's Garden of Eden Addition to Seattle	
	Lot 46, Block A. Div. 1. Kennydale.	
	(Frame hotel bldg. & store)	962.00
"	Lot 12, Block 7, 323 West Mercer Street, No. 10 ft. of,	
	Lot 13, Block 7, all of.	
	Lot 14, Block 7, re-plat of Blks. 1, 2, 6, 7, 13, 14 and 23 of N. Seattle	
	(2 story 8-room frame bldg. & 1-story 5-room bldg.)	6,589.70
"	Lot 14, Block 2, Clairmont Addition	
	Lot 15, Block 2, Clairmont Addition	
	(Unimproved)	500.00

State and County where located	Description of Property	Valuation upon July 31, 1932, Balance Sheet, Pacific Products, Inc.
State of Washington		
King	Lot 1, Block 60, Maynard's Lake Washington Add.	
	Lot 2, Block 60, Maynard's Lake Washington Add.	
	Lot 11, Block 60, Maynard's Lake Washington Add.	
	Lot 12, Block 60, Maynard's Lake Washington Add.	
	(Unimproved)	1.00
"	Lot 37—Block 402 Seattle Tide Lands	3,532.92
"	Lot 1—Sprague's Addition, except portion conveyed to Puget Sound Railway, April 6, 1906	7,970.97
Benton	Kennedy's 1st Add'n. Town of Kiona, Wash. Lots 12, 13, 5, Block 5	75.00
Province of Canada		
Saskatchewan	N ½ of Sec. 21—TWP 33, R5W of (320 acres) 2nd M	
Province of Alberta	Prairie lands—The NE ¼ of Sec. 35 TWP 52 R 3 W 5 M (160 acres) being part of Wabamum Indian Reserve	10,395.30
" " "	The SE ¼ of Sec. 21—TWP 53—R 19 W 4 M (160 acres) (prairie lands).	
State of Washington		
Stevens	The NE ¼ of Sec. 15 in TWP 29 NR 36 E W M Farm Lands containing 160 acres more or less	2,000.00
State of Montana		
Powell	Storage Bldg. Original townsite of Deer Lodge, Lot 1, Block 9	1,800.00
State of Washington		
Douglas	1-story brick building, original Gov't. Townsite of Waterville Lot 1, Block 8	1,500.00
	2nd Addition to Waterville Lots 6 to 10 Blk. 28	938.72

State and County where located	Description of Property	Valuation upon July 31, 1932, Balance Sheet, Pacific Products, Inc.
State of Washington		
Benton	Bldg. used as Blacksmith shop N. 114 ft. of N.P. Irrigation Co.'s 1st add'n. to Kennewich measured along the west side of said lot—Lot 12, Block 2	1,500.00
Whatcom	York addition to City of New Whatcom (now Bellingham) Lot 10, Block 18	350.00
Adams	The SW ½ front and rear of original Town of Ritzville, Lot 8, Block 10	500.00
Whatcom	Old Stg. Bldg. Good only for Lbr. Johnson's add'n. to Sumas Lot 6, Block 1	1,489.15
Lincoln	Beer Stg. Whse. SE add'n. to Town of Davenport excepting coal shed now located on premises. N 50 ft. sold March 19, 1908 for $75.00. Co. now owns So. 50 ft. Lot 10, Block 16	650.00
Yakima	N ½ of NW ¼ and W ½ of SW ¼ of Sec. 34 TWP 13 N R 20 E W M 16 acres	2,755.73
State of Arizona		
Yavapai	Frame Stge. Bldg. Moeller add'n. to City of Prescott. Lot 21, Block 13	2,000.00
State of Washington		
Jefferson	Irondale, Lot 55, Block 46 (Bldg. sold off this property)	1.00
Kitsap	Manchester Heights—Unimproved (replat of) Lot 1, Block 16	20.00
"	Dane Acreage N.W. ¼ of SW ¼ and approx. 63½ acres (shack) Lot 3, Sec. TP. R. Acres 17 24 N1. E WM 63½	4,000.00
Yakima	E. ½ of the NE ¼ of the NE ¼ of Sec. 9, Tp. 14 R. 19 E Acres—WM 20 Unimproved	40.00

State and County where located	Description of Property	Valuation upon July 31, 1932, Balance Sheet, Pacific Products, Inc.
State of Washington		
Kittitas	Brick Bldg. All that portion of original town of Ellinsburg, com. at a pt. 30 ft. So. of N.W. corner of Lot 4 running thence East 120 ft. parallel with the N. line of said lot 4 thence So. 30 ft. thence W. 24 ft. thence So. 60 ft. thence W. 48 ft. thence N 66 ft. thence W. 48 ft. thence N. 24 ft. to place of beginning. Lots 4, 5, Block 15	8,757.82
State of California		
San Joaquin	City of Stockton. The E 15 ft. of the W 40 ft. of Lot 4, Blk. 253 and the E 10 ft. of Lot 4, Blk. 253 and the W 40 ft. of Lot 6, Blk. 253	11,371.92
	East of Center Street, according to the official Map or plat in the City of Stockon.	
State of Washington		
King	Lots 8 to 22, inclusive, Block 2	
	That portion of lots 8 to 22 both incl. and that portion of the alley vacated by Ord. 410 within the boundaries of said lots Blk. 2, Carsten's Add. to City of Georgetown (now Seattle) that lies E. of the 10 ft. strip of said blk. deeded to Georgetown by the O & W Ry. for the widening of Charleston St. now Corson Ave. containing 0.93 acres, more or less.	
	Excepting therefrom a strip of land 45 ft. in width, the center line of which is described as follows:	
	Beg. at a pt. on the S. line of Norton St. now Vale St., 31.15 ft. Wstly from the NE cor. of Lot 2, Blk. 1 subdivision of Julius Horton tracts Nos. 13 and 14, Georgetown; th. NWstly 1075 ft. more or less to pt. on the W. line of Charleston St. now Corson Ave., Situated 32.47 ft. Nthly from the S.E. Cor. of Lot 14, Blk. 7, King County Add. to Seattle.	
	(Garage and magnesia pipe covering	

State and County where located	Description of Property	Valuation upon July 31, 1932, Balance Sheet, Pacific Products, Inc.
State of Washington		
King	Lot 9, Blk. 17, Tp. 24, R. 4	
	Beg. at pt. 90 ft. SE of N.W. Cor. of Lot 9 of the tracts of Julius Horton for true pl. of beg. th. 161 ft. NEstly to NE boundary line of said lot, the. SE along said boundary line, 30 ft. th. SW. 161 ft. to the County Road; the. NW 30 ft. to pl. of beg.	
	Also a tract of land described as follows: Beg. at a pt. 120 ft. SE of NW cor. of lot 9 of plat of Tracts of Julius Horton, and along the line of said lot to true pl. of beg.; the NE 160 ft. to E. boundary line of said lot; th. SE 30 ft. along E. Boundary line of said lot; th. SW 160 ft. to W. boundary line of said lot; th. NW 30 ft. to pl. of beg.	
	(California Cotton Mills Location)......	7,003.34
Skagit	Tax lot #3 Section 25 Township 34—R 4 E W M 0.11 Acres	25.00
	Total	$178,776.54

EXHIBIT D

This Indenture, made the eleventh day of October in the year one thousand nine hundred and thirty-two, between Pacific Products, Inc., a corporation duly organized and existing under and by virtue of the laws of the State of California and having its principal office for the transaction of business in the City and County of San Francisco, State of California, the party of the first part, and Rainier

Brewing Company, Inc., a like corporation, having its principal office for the transaction of business in the City and County of San Francisco, State of California, the party of the second part,

Witnesseth:

That the party of the first part, in consideration of the sum of ten ($10.00) dollars lawful money of the United States of America, to it in hand paid by the said party of the second part, the receipt whereof is hereby acknowledged, does by these presents grant, bargain and sell unto the said party of the second part, its successors and assigns, forever, all those certain lots, pieces or parcels of land bounded and described as follows, to-wit:

> All that certain lot, piece or parcel of land situate in the City and County of San Francisco, State of California, described as follows, to-wit:
>
> Beginning at the point of intersection of the westerly line of Bryant Street with the southerly line of Alameda Street and running thence southerly along the westerly line of Bryant Street 324′-9″ to a point distant 73′-3″ northerly from the northerly line of 15th Street, and running thence westerly 204′-6″ to a point on the easterly line of Florida Street, distant northerly thereon 118′-0″ from the northerly line of 15th Street, and running thence northerly along the easterly line of Florida Street 282′-0″ to the southerly line of Alameda Street

and running thence easterly [84] along the southerly line of Alameda Street 200′-0″ to the point of beginning;

Being a portion of Potrero Block 24.

Also,

All the following described property situate in the City of Seattle, County of King, State of Washington:

A tract of land comprising portions of tracts 8 and 9 of the Julius Horton tracts recorded in Vol. 3 of Plats, page 171, records of King County, Washington, also an unplatted tract of land situated in the L. M. Collins Donation Claim lying between the easterly line of said tract 8 of the Julius Horton tracts and the northerly line of former Nora Street in Sprague's Addition to the City of Seattle as recorded in Vol. 7 of Plats, page 49, records of King County, Washington, also portion of vacated Nora Street as vacated by Ordinance No. 78, City of Georgetown, also portion of Block 1, Sprague's Addition, and vacated alley in said block, also vacated portion of Juneau Street as vacated by Ordinance No. 35490, City of Seattle, the boundaries of said tract of land are more particularly described as follows:

Commencing at the monument marking the intersection of the west line of the said Julius Horton Tracts and the center line of Duwamish Avenue; thence S. 34° 23′ 39″ E. along said

center line 187.95 feet; thence N. 55° 36′ 21″ E. 30 feet to the easterly margin of Duwamish Avenue and the true place of beginning; thence S. 34° 23′ 39″ E. along said easterly margin 1449.08 feet; thence continuing along the northerly margin of Duwamish Avenue, S. 66° 47′ 45″ E. 38.19 feet; thence S. 70° 45′ 34″ E. 44.91 feet to the northwesterly margin of the unvacated portion of Juneau Street, as the same is set forth in Ordinance No. 35490 of Seattle; thence N. 53° 41′ 06″ E. 123.86 feet along said Juneau Street margin; thence S. 80° 22′ 34″ E. 33.58 feet along the northerly margin of Juneau Street; thence N. 53° 41′ 06″ E. 7.18 feet along said margin of Juneau Street; thence N. 36° 18′ 54″ W. 1472.41 feet to point of curve; thence to the right on a curve of 5977.22 feet radius 64.85 feet; thence S. 55° 36′ 21″ W. 151.00 feet to the place of beginning.

Together with the tenements, hereditaments, and appurtenances thereunto belonging or appertaining, and the reversion and reversions, remainder and remainders, rents, issues, and profits thereof. [85]

To Have And To Hold the said premises, together with the appurtenances, unto the said party of the second part, and to its successors and assigns, forever.

In Witness Whereof, the party of the first part has hereunto signed its named and affixed its cor-

porate seal, by its officers thereunto duly authorized, the day and year first hereinabove written.

[Seal] PACIFIC PRODUCTS, INC.,

By /s/ LOUIS HEMRICH,
President.

By /s/ F. J. McCARTHY,
Secretary.

(U. S. Internal Revenue Stamps in the amount of $1009.00 were affixed to the original of this instrument and canceled as of the 11th day of October, 1932.) [86]

State of California,
City and County of San Francisco—ss.

On this 11th day of October, in the year one thousand nine hundred and thirty-two, before me, James F. McCue, a Notary Public in and for the City and County of San Francisco, State of California, residing therein, duly commissioned and sworn, personally appeared Louis Hemrich and F. J. McCarthy, known to me to be the President and Secretary, respectively, of Pacific Products, Inc., the corporation that executed the within instrument, and known to me to be the persons who executed the within instrument on behalf of the corporation therein named, and acknowledged to me that such corporation executed the same.

In Witness Whereof, I have hereunto set my hand and affixed my Official Seal, at my office, in

the City and County of San Francisco, the day and year in this certificate first above written.

[Seal] /s/ JAMES F. McCUE,
Notary Public in and for the City and County of San Francisco, State of California.

State of California,
City and County of San Francisco—ss.

On this 11th day of October, in the year one thousand nine hundred and thirty-two, before me personally appeared Louis Hemrich and F. J. McCarthy, to me known to be the President and Secretary, respectively, of Pacific Products, Inc., the corporation that executed the within and foregoing instrument, and acknowledged the said instrument to be the free and voluntary act and deed of said corporation, for the uses and purposes therein mentioned, and on oath stated that they were authorized to execute said instrument and that the seal affixed is the corporate seal of said corporation.

In Witness Whereof, I have hereunto set my hand and affixed my official seal the day and year first above written.

[Seal] /s/ M. V. COLLINS,
Commissioner of Deeds for the State of Washington with offices at 433 California Street, San Francisco, California.

Filed July 19, 1945. [87]

[Title of Tax Court and Cause.]

STIPULATION II

It is hereby stipulated and agreed by and between the parties hereto, through their respective counsel:

That during the period from July 1, 1935 to and including June 30, 1940, Seattle Brewing & Malting Co. (formerly Century Brewing Association) sold in the State of Washington and the Territory of Alaska the following quantities of beer, ale and other alcoholic malt products under the name "Rainier" and paid as royalties thereon the following amounts:

Year Ending June 30th	Royalties	Barrels
1936	$ 75,000	60,171
1937	75,000	82,881
1938	85,731.12	114,308.16
1939	84,403.63	112,538.14
1940	98,834.47	131,355.89
Total	$418,969.22	501,253.89

/s/ A. CALDER MACKAY,

/s/ ADAM Y. BENNION,

Counsel for Petitioner

Of Counsel:

/s/ F. SANFORD SMITH,

/s/ CLIFFORD J. MacMILLAN,

/s/ O. J. SONNENBERG,

/s/ SCOTT H. DUNHAM.

/s/ J. P. WENCHEL BHN

Chief Counsel, Bureau of Internal Revenue,

Counsel for Respondent.

Filed July 19, 1945. [89]

[Title of Tax Court and Cause.]

STIPULATION III

It is hereby stipulated and agreed by and between the parties hereto, through their respective counsel, that—

I.

Petitioner's predecessors, Seattle Brewing and Malting Co. (the West Virginia corporation) and Rainier Brewing Company (the Washington corporation) filed income tax returns for the years 1918, 1919 and 1920, but claimed no deductions therein for obsolescence of good will or trade names.

II.

In July, 1920, Seattle Brewing and Malting Co. (the West Virginia corporation) filed a claim for abatement of taxes for the year 1919, a photostatic copy of which is attached hereto, marked Exhibit I and made a part hereof.

III.

The Commissioner of Internal Revenue thereafter, in 1924, in lieu of the amount of $542,240.27 stated in Schedules E and F of Exhibit I attached hereto, computed an amount of $406,680.20, which was arrived at by using the same figures as those used in Exhibit I attached hereto, but changing the capitalization rate from 15 per cent, as used in Exhibit I, to 20 per cent. [90]

Method Used in Valuing Good Will

The only basis for establishing a rate of capitalizing the good will value of the company is given in Bulletin 10-20-777-ARM 34- of Income Tax Rulings, wherein it is provided that earnings for tangible and intangible assets should be taken over a period of [92] not less than five years prior to March 1, 1913. As indicated in schedules attached, the earnings of this Corporation have been taken from the inception of the business, 1903 to March 1, 1913. It is believed that this longer period truely reflects the earning capacity and invested capital of the business on which to base normal and excess over normal earnings for the purpose of establishing good will.

In preparing this claim the normal earnings have established at ten per cent of the average invested capital prior to March 1, 1913 and the excess of actual earnings over this amount capitalized at 15 per cent to establish good will loss.

The claimant contends that the business conducted is not of a hazardous nature, and is entitled to the lowest possible rate for a basis of capitalization of its intangibles.

The schedules submitted show a substantial business throughout the entire period of its existence and the above method applied does not produce a result that compensates for the actual loss sustained.

Its loss is irreparable and the amount here asked is very small for the great loss of an established industry.

Schedules in Support of Claim

1. Schedule "A" Balance Sheets.

2. Schedule "B" Summary (Capital, operations, surplus)

3. Schedule "C" Analysis operating expenses.

4. Schedule "D" Analysis surplus 6-30-13 to 12-31-19.

5. Schedule "E" Computation of good will loss.

6. Schedule "F" Application of good will loss to taxes assessed.

Respectfully submitted. [93]

ETS

6 18	7 1909
50.06	205483
42.54	34858
03.10	12411
72.73	6786
19.36	50884
80.17	86824
85.00	31112
23.81	1458
76.77	429818
37.09	6896
00.00	22270
47.37	2584
85.00	31112
40.80	935
83.39	21051
96.06	5723
00.00	2000000
87.06	139245
76.77	429818

SCHEDULE "A"—BALANCE SHEETS

(Fiscal Year ending June 30th)

Assets	1 1903	2 1904	3 1905	4 1906	5 1907	6 1908	7 1909	8 1910	9 1911	10 1912	11 1913
Const. & Property	1367213.76	1456212.21	1584584.41	1679821.75	1911722.07	2034350.06	2054831.60	2125021.28	2221883.35	2306552.39	2157882.16
Equipment	186425.35	223051.27	210191.82	213487.03	314587.96	339942.54	348585.40	322917.14	315962.89	316263.31	307836.34
Investments	36159.54	16981.46	12233.35	22322.21	24352.29	71403.10	124113.38	129652.79	111500.63	106865.75	105237.72
Cash	9579.11	19952.15	38892.70	34719.72	36721.74	11272.73	67866.07	29710.44	77451.68	69686.13	61362.15
Material & Supplies	234966.50	288004.54	318986.36	314200.55	445769.97	515719.36	508844.60	477654.24	53,9692.08	677860.43	746064.66
Accounts Receivable	606011.53	667493.24	585312.87	651792.35	792932.47	738880.17	868243.59	934643.71	1002358.63	1144618.19	1154799.94
Accommodation Notes	77758.74	91571.70	84047.70	177125.00	168726.01	203285.00	311120.00	205470.00	227994.30	154590.00	158384.00
Prepaid Expenses	8098.01	10169.83	8559.51	19335.42	16146.58	15423.81	14580.84	14984.38	16016.01	14337.74	5202.33
Total	2526212.54	2773436.40	2842808.72	3112804.03	3710959.09	3930276.77	4298185.48	4240053.98	4512859.57	4790773.94	4696769.30
Liabilities											
Audited Vouchers	83420.27	83945.83	78101.53	84143.55	189961.63	68437.09	68967.78	60980.05	65776.23	122714.76	90546.22
Notes Payable	263000.00	286500.00	239000.00	166700.00	292200.00	322200.00	222700.00	79000.00	....	57500.00	156500.00
Accounts Payable	14790.85	6062.19	5760.93	3702.90	14632.78	18247.37	25842.10	26938.60	87460.80	37148.49	33420.00
Accommodation Notes	77758.74	91571.70	84047.70	177125.00	168726.01	203285.00	311120.00	205470.00	227994.30	154590.00	158384.00
Accrued Expense	6304.71	7976.52	3856.80	6933.55	7635.66	6340.80	9353.74	5229.52	6301.94	7202.60	17672.52
Depreciation Reserve	113432.53	139245.80	150000.00	170997.60	191442.57	190383.39	210513.44	243301.24	284087.97	319230.95	357654.55
Bad Debts Reserve	12269.83	10521.04	5000.00	4873.28	35957.40	48296.06	57230.32	45266.90	38059.87	49435.60	31424.22
Capital Stock	1000000.00	1000000.00	1000000.00	1000000.00	1000000.00	2000000.00	2000000.00	2000000.00	2000000.00	2000000.00	3000000.00
Surplus	955235.61	1147613.32	1277041.76	1498328.15	1810403.04	1073087.06	1392458.10	1573867.67	1803178.46	2042951.54	851167.79
Total Liabilities and Capital	2526212.54	2773436.40	2842808.72	3112804.03	3710959.09	3930276.77	4298185.48	4240053.98	4512859.57	4790773.94	4696769.30

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SCHEDULE "B"

Summary operating and surplus analysis

(Fiscal year ending June 30th)

	1 1903	2 1904	3 1905	4 1906	5 1907	6 1908	7 1909	8 1910	9 1911	10 1912	11 1913	12 8/12 of 1913	13 Average
1. Inventory 1st of Yr.	285834.46	234966.50	288004.54	318986.36	314200.55	445769.97	515719.36	508844.60	477654.24	539692.08	677860.43		
2. Purchases	262727.07	232058.11	200110.71	204499.42	440597.58	252518.49	173721.27	349904.49	500233.78	521467.80	648092.12		
3. Total	548561.53	467024.61	488115.25	523485.78	754798.13	698288.46	689440.63	858749.09	977888.02	1061159.88	1325952.55		
4. Inventory End of Yr.	234966.50	288004.54	318986.36	314200.55	445769.97	515719.36	508844.60	477654.24	539692.08	677860.43	746064.66		
5. Cost goods sold	783528.03	755029.15	807101.61	837686.33	1200568.10	1214007.82	1198285.23	1336403.33	1517580.10	1739020.31	2072017.21		
6. Gross Sales	1447043.68	1430253.50	1442917.37	1493190.53	2164916.95	2169353.18	2091570.58	2321822.35	2596459.83	2873603.62	3213130.07		
7. Gross Profits	663515.65	675224.35	635815.76	655504.20	964348.85	955345.36	893285.35	985419.02	1078879.73	1134583.31	1141112.86		
8. Other Income	20847.38	....	....	58784.97	3093.55	13312.54	112672.78	15165.33	66166.23	19586.19	24700.07		
9. Gross Income	684363.03	675224.35	635815.76	714289.17	967442.40	968657.90	1005958.13	1000584.35	1145045.96	1154169.50	1165812.93		
10. Expenses	307317.02	407732.26	376955.01	375312.30	485602.28	541363.21	513167.02	583052.43	607994.67	604863.99	633611.14		
11. Advertising	47305.92	40361.75	44194.74	57690.48	79765.23	62110.67	53420.07	61122.35	67740.50	69532.43	95244.73		
12. Total	354622.94	448094.01	421139.95	433002.78	565367.51	603473.88	566587.09	644174.78	675735.17	674396.42	728855.87		
13. Net Income	329740.09	227130.34	214675.81	281286.39	402074.89	365184.02	439371.04	356409.57	469310.79	479773.08	436957.06	291304.71	361524.44
14. Inv. Capital 1st Yr.	1685495.52	1955235.61	2122365.95	2277041.76	2498328.15	2810403.04	3073087.06	3392458.10	3573867.67	3803178.46	4042951.54	2695301.03	2801884.00
15. Total	2015235.61	2182365.95	2337041.76	2558328.15	2900403.04	3175587.06	3512458.10	3748867.67	4043178.46	4282951.54	4479908.60		
16. Dividends Paid	60000.00	60000.00	60000.00	60000.00	90000.00	102500.00	120000.00	175000.00	240000.00	240000.00	628740.81		
17. Inv. Cap. End Yr.	1955235.61	2122365.95	2277041.76	2498328.15	2810403.04	3073087.06	3392458.10	3573867.67	3803178.46	4042951.54	3851167.79		

7 1909	8 1910	9 191
0840.64	163359.37	200513
6168.83	75936.61	84920
0762.81	109566.88	115976
8401.52	75098.49	60714
8006.21	....	....
....	....	....
1718.25	11777.99	12078
6000.00	36000.00	36000
....	1468.30	1972
7598.96	94353.78	79248
3669.80	12440.97	12536
....	3050.04	4032
3167.02	583052.43	607994
3420.07	61122.35	67740
6587.09	644174.78	675735

SCHEDULE "C"

Analysis of operating expenses

	1 1903	2 1904	3 1905	4 1906	5 1907	6 1908	7 1909	8 1910	9 1911	10 1912	11 1913
1. Wages	121262.40	136081.85	130316.55	139446.03	205898.12	171639.84	160840.64	163359.37	200513.78	236510.42	253026.90
2. Salaries	30646.26	32010.02	36859.80	40531.55	46966.56	64076.64	76168.83	75936.61	84920.45	84391.66	89698.69
3. General Office	32690.89	34596.66	32987.19	57987.13	67454.86	76553.04	70762.81	109566.88	115976.73	102280.11	116435.19
4. Other Expenses	31717.23	34905.62	37482.63	28048.94	55487.68	98729.79	88401.52	75098.49	60714.55	24076.28	29774.01
5. Interest	12841.30	18538.74	17760.88	13861.34	9815.59	19144.17	8006.21	....	....	....	....
6. Rentals	391.23	1058.34	6901.98	7480.38	....	....	....	....	....	4798.73	....
7. Insurance	15438.36	15843.20	13734.78	14539.14	13405.62	11810.24	11718.25	11777.99	12078.98	11112.18	12248.36
8. Bad Debts	11000.00	85794.46	52974.27	24000.00	33000.00	36000.00	36000.00	36000.00	36000.00	36000.00	36000.00
9. Repairs	8662.05	5795.67	932.25	1376.30	....	578.34	....	1468.30	1972.21	6485.06	....
10. Depreciation	34988.98	32632.38	35598.96	35598.96	44598.96	47598.96	47598.96	94353.78	79248.84	79728.84	79728.84
11. Taxes	7678.32	10478.32	11395.62	12442.53	8974.89	15232.19	13669.80	12440.97	12536.58	14879.39	12701.11
12. Income Taxes	....	....	....	....	....	....	....	3050.04	4032.55	4601.32	3998.04
13. Sub-Total	307317.02	407732.26	376945.21	375312.30	485602.28	541363.21	513167.02	583052.43	607994.67	604863.99	633611.14
14. Advertising	47305.92	40361.75	44194.74	57690.48	79765.23	62110.67	53420.07	61122.35	67740.50	69532.43	95244.73
15. Total	354622.94	448094.01	421139.95	433002.78	565367.51	603473.88	566587.09	644174.78	675735.17	674396.42	728855.87

SCHEDULE "D"

(Analysis of surplus June 30, 1913 to December 31, 1919)

June 30, 1913, Surplus		851,167.79
Earning June 30, 1913 to June 30, 1914		659,965.66
		1,511,133.45
Less Dividends Paid		300,000.00
June 30, 1914 Surplus		1,211,133.45
Earning June 30, 1914 to June 30, 1915		556,077.56
		1,767,211.01
Less Dividends Paid		300,000.00
June 30, 1915 Surplus		1,467,211.01
Earning June 30, 1915 to June 30, 1916		154,611.67
		1,621,822.68
Less Dividends Paid	180,000.00	
Less Plant Obsolescence	900,474.20	1,080,474.20
		541,348.48
Earnings June 30, 1916 to June 30, 1917		97,485.85
		638,834.33
Less Dividends Paid		180,000.00
June 30, 1917 Surplus		458,834.33
Earnings June 30, 1917 to June 30, 1918		108,664.39
		567,498.72
Less Dividends Paid		180,000.00
		387,498.72
Earnings June 30, 1918 to June 30, 1919		248,525.65
		636,024.37
Less Dividends Paid		180,000.00
		456,024.37
Earnings June 30 to December 31, 1919		53,405.47
December 31, 1919 Surplus		$ 509,429.84

[97]

SCHEDULE "E"

(Computation of Good Will Loss)

Average capital invested prior to March 1, 1913 (Schedule B, Line 14, Column 13)			$2,801,884.00
Average Earnings prior to March 1, 1913. (Schedule B, Line 13, Column 13)	$361,524.44		
Average normal earning of invested capital prior to March 1, 1913 @ 10%	$280,188.40		
Average Good Will earnings prior to March 1, 1913	$ 81,336.04		
Average yearly earnings of Good Will prior to March 1, 1913 capitalized @ 15%		$542,240.27	
Net profits for year 1918	None		
Normal earnings of year 1918 ($4,160,575.64 @ 10%)	$416,057.64		
The present value of earnings attributable to good will January 31, 1918	None		
Computable value of Good Will loss applicable to 1919 and future income		$542,240.27	

SCHEDULE "F"

(Application of Good Will loss to taxes assessed.)

Computable value of Good Will loss (Schedule "E")			$542,240.27
Net taxable income as per return of income for year 1919		$174,188.84	
Amount of Good Will loss applied to above income		$174,188.84	
Amount of taxes assessed on above income	$16,725.28		
Amount asked to be abated as per claim in abatement filed herewith (Form 47) (Temporary claim in abatement filed May 15, 1920 is hereby cancelled)	$16,725.28		
Remaining balance of Good Will loss			$368,051.33

Filed July 19, 1945.

Before the Tax Court of the United States

Docket No. 4895

In the Matter of:

RAINIER BREWING COMPANY,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

July 19, 1945—10:15 A.M.

Before: Honorable Marian J. Harron, Judge.

Appearances:

A. Calder Mackay, Esq., 728 Pacific Mutual Building, Los Angeles, California, appearing on behalf of Rainier Brewing Company, Petitioner.

Adam Y. Bennion, Esq., 728 Pacific Mutual Building, Los Angeles, California, appearing on behalf of Rainier Brewing Company, Petitioner.

F. Sanford Smith, Esq., 705 Standard Oil Building, San Francisco, California, appearing on behalf of Rainier Brewing Company, Petitioner. [103]

Clifford J. MacMillan, Esq., 705 Standard Oil Building, San Francisco, California, appearing on behalf of Rainier Brewing Company, Petitioner.

O. J. Sonnenberg, Esq., Crocker Building, San Francisco, California, appearing on behalf of Rainier Brewing Company, Petitioner.

Scott H. Dunham, Esq., Crocker Building, San Francisco, California, appearing on behalf of Rainier Brewing Company, Petitioner.

B. H. Neblett, Esq., (Honorable J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue), appearing on behalf of the Commissioner of Internal Revenue, Respondent. [104]

PROCEEDINGS

The Clerk: Docket No. 4895, Rainier Brewing Company.

Will you state your appearances for the record, please?

Mr. Mackay: A Calder Mackay, Adam Y. Bennion, F. Sanford Smith, Clifford J. MacMillan, O. J. Sonnenberg and Scott H. Dunham for Petitioner.

Mr. Neblett: B. H. Neblett, appearing for the Respondent.

The Court: Mr. Mackay, will you make your statement?

Are you going to present the whole case yourself?

Mr. Mackay: Yes.

The Court: You have a distinguished array of associates.

Opening Statement on Behalf of the Petitioner

By Mr. Mackay:

Mr. Mackay: If your Honor please, the taxable years involved in the appeal in this case are the calendar years 1940 and 1941.

The Petitioner has decided to abandon the issue in 1941, which has to do with the abandonment loss of some neon signs.

For the year 1940, substantial taxes are involved, [105] namely, approximately $235,000 in income taxes, declared value excess profits taxes in the round figure of $18,000, and excess profits tax of approximately $286,000, or a total for the year 1940 of approximately $539,000.

All substantial taxes for 1940, except a small amount of excess profits tax, are attributable to the determination by the Commissioner that promissory notes in the amount of $1,000,000 received by the taxpayer during the year 1940 constituted taxable ordinary income.

The Petitioner challenges this determination, principally on the ground that the $1,000,000 in notes constitutes a return of capital rather than ordinary income. The taxpayer takes the position that the notes were the proceeds from the sale of a capital asset having a basis of $1,000,000, so that no gain was realized therefrom.

We have some alternative grounds, however, if your Honor please. If the Court should hold that the transaction which I shall presently describe did not constitute a sale, the taxpayer contends that nevertheless the $1,000,000 notes constitute a recovery of capital and should be applied against and reduce the basis of the property in question.

The taxpayer relies upon another alternative ground, demonstrating that the Commissioner's determination was erroneous, but before stating that I

think I ought to outline the facts that we rely upon. [106]

The Petitioner, Rainier Brewing Company, is a successor corporation of a company which began in 1893 to manufacture and sell alcoholic malt beverages under the trade name "Rainier."

I might state that there have been several reorganizations of the company since that time. These reorganizations, of course, are significant only because Petitioner's basis, what we contend it sold in 1940, is the March 1, 1913 value.

I might state for your Honor that we have a stipulation regarding various reorganizations which will show that they are tax free reorganizations. So that, I think if we do determine it to be a sale, we will establish that fact as a cost.

In order that there shall be no confusion, however, resulting from the change in names through these reorganizations, we have prepared a chart of the corporate history, and we should like to submit this to your Honor, because there may be a little confusion.

Your Honor will note it was the original company that was known as the Seattle Brewing and Malting Company that was organized in 1893 and incorporated until about 1903. That was a Washington corporation. At that time there was a West Virginia corporation organized by the same name, but just a little different in spelling. The latter company carried on the business, then from 1903 until 1925, when all the business was transferred to a California corporation known as the Pacific Products, Inc., which was organized for that purpose. The business

was thereafter transferred to Rainier Brewing Company, organized in California in 1932, which latter company merged into Pacific Products, Inc., in 1937, to form the present taxpayer, under the name of "Rainier Brewing Company."

But, as I have stated, beginning in 1893, beer, ale and other alcoholic malt beverages were manufactured by the predecessor in Seattle, Washington, and prior to 1913 were distributed principally in the State of Washington, in fact, if your Honor please, is submitted in the pleadings. There were also some products shipped to points outside of the State of Washington.

The evidence in short, your Honor please, is that the business was eminently successful, and advertising created a great demand for the beer known as "Rainier beer."

As I have stated, Petitioner contends that a very substantial value was built up for the name "Rainier" at March 1, 1913, and we contend that that is at least $1,000,000.

In 1935 a contract was entered into between Rainier and a competitor known as the Century Brewing Company. The contract recited that Rainier was the owner of a brewing plant in Seattle, of the trade names "Rainier" and "Tacoma," [108] and that "said names are well and favorably known." The contract is rather lengthy, but the gist of it was that Rainier sold to Century for specified considerations its Seattle plant, together with beer on hand and miscellaneous equipment, and Rainier withdrew from the sale of its alcoholic malt prod-

ucts in the State of Washington and the Territory of Alaska. By the terms of the contract, Rainier granted to Century the sole and exclusive perpetual right and license to manufacture and market beer, ale and other alcoholic malt beverages within the State of Washington and the Territory of Alaska under the trade names of "Rainier" and "Tacoma," according to the formulas they passed along with the names.

The contract also provided that Century, for the right and license that it granted, would pay Rainier a royalty of seventy-five cents per barrel up to 125,000 barrels annually, and thereafter eighty cents per barrel for all products sold in the names of the territory designated, with a minimum annual payment, however, of $75,000.

If your Honor please, the parties, the evidence will show, operated under this agreement from 1935 to 1940, and that royalties were paid by Century to Rainier, and the contract also provided (I refer particularly to paragraph 13) that after it had been in effect for five years, Century should have the option of electing to terminate all royalties thereafter payable under the contract by delivering to Rainier [109] five promissory notes aggregating $1,000,000.

On July 1, 1940, Century exercised that option and delivered to Rainier $1,000,000 in notes, which we have stated the Commissioner treated as ordinary income, and, we are contending, were the proceeds of sale.

Your Honor please, there are many provisions in the contract which have a bearing on this inter-

pretation. The Commissioner apparently takes the view that the $1,000,000, since the contract speaks of terminating royalties, constitutes in effect a prepayment of royalties. The taxpayer maintains, however, upon the authority of Parke-Davis & Co., 31 BTA 421, and other bases, and also by reason of the nature of the trade name, that there was for all practical purposes a sale in 1940 by Rainier of its trade name, "Rainier," in the State of Washington and Territory of Alaska.

The evidence will show that although this contract covers the trade name "Rainier" and "Tacoma," that in effect "Tacoma" was of very minor significance. Very few sales were made by the taxpayer under that name prior to 1935, and it is admitted in the pleadings that after that there were no sales made at all by the acquiring company, Century.

We think, if your Honor please, that this petitioner's position that the trade name and good will associated were sold in 1940 is confirmed by many provisions of the contract. I will just take a minute to indicate some of those [110] provisions.

For example, Century was required to give Rainier a mortgage on the property, on the brewing plant, to secure the performance of Century's obligation under the contract, or, if it should sell the plant, it was required to impound at least $250,000 proceeds as security.

This evidence will show also that this mortgage was satisfied, and that the present relationship was released when the notes were finally paid.

Also, there is another provision, that prior to the

exercise of the option, the royalties payable by Century would have been deferred by reason of strikes, Acts of God, earthquakes, or things like that, for the period in which these events occurred. We think that is material. We want to point out that after the exercise of the option there was no condition like that at all, that the full "burdens of ownership," if you can call them that, as well as the benefits of ownership, were in Century, that if there was a strike, earthquake or Act of God, the loss fell upon Century. Prior to that, it fell upon Rainier.

We also rely upon the case of the Board of Tax Appeals, Hammond Lumber Company 352.

So, it is our position, if your Honor please, that the contract was a royalty contract for a period of five years, with an option to purchase, and that in 1940 the option was [111] exercised and by that exercise the licensing provisions of the contract were terminated and its obligation of maintaining a mortgage on the property was terminated, its obligation to impound funds was terminated, its obligation to render monthly and annual statements was terminated, its obligation to turn over the proceeds upon sale of the property terminated, and Rainier's right to terminate the contract because of Century default was likewise terminated.

We might mention the fact to your Honor that the Century Brewing Association, which is the party to this contract, under the contract itself was permitted to change its name to the Seattle Brewing & Malting Company, and that is why we put that diagram up there, so there would be no confusion.

I might state that we recognize the Commissioner of Internal Revenue has the right to take inconsistent positions. I might state that the Commissioner has taken the position in another case already submitted to the Tax Court that this was a sale and not a prepayment of royalty. I wish to say that I thoroughly agree with the position the Commissioner took there. I compliment him on his very able presentation of the law and his very able brief. I am glad to agree with the Commissioner in that respect.

The Court: That is the case that was tried in Seattle on the last calendar, before Judge Mellott, is that [112] right?

Mr. Mackay: That is right, your Honor.

One other thing I wanted to point out: it should be noted that if a transaction is held to be a sale, then no part of the gain will be subject to profits tax, for Section 721 of the Code so provides. However, if the Court should be of the opinion that the transaction did not constitute a sale, the taxpayer contends that in the alternative the notes of $1,000,000 constitute a return of capital. Also, where it is well settled that the Internal Revenue Code does not define what is a return of capital and what is income, the decision of course is left to the Court.

I might state as a further alternative issue, the Petitioner contends that if it is held that notes constitute ordinary income, it is entitled to a deduction for the exhaustion there during 1940, and another alternative position is that if it is held to be an ordinary income, then none of that would be

subject to excess profits tax because it would be abnormal income within the provisions of Section 721 of the Internal Revenue Code.

I think that is all.

The Court: Mr. Neblett?

Opening Statement on Behalf of the Respondent By Mr. Neblett:

Mr. Neblett: May it please the Court, the taxes [113] in controversy are income and declared value excess profits taxes, and excess profits taxes for the calendar year 1940 in the respective amounts of $235,321.78, $18,617.60, and $285,948.74, for the year 1940, and excess profits tax for 1941 of $26,119.93.

The issue with respect to 1941 has been abandoned by the Petitioner, so that the deficiency for that year would be the $26,119.93.

Your Honor, the total deficiencies are approximately $566,008.04.

As we understand it, the issues are:

1. Whether the Petitioner derived ordinary income in the amount of $1,000,000 in the calendar year 1940, or was said amount the proceeds from the sale of a capital asset in said year?

2. Whether the Petitioner is entitled to use the March 1, 1913 value of the "right" transferred on July 1, 1940, and if so, what is the March 1, 1940 value of such "right?"

3. Whether any part of the $1,000,000 received by Rainier Brewing Company is abnormal income attributable to years prior to 1940 within the meaning of Section 721 of the Internal Revenue Code?

Your Honor please, the government's theory on

these issues is as follows: that the transaction of 1940 was a [114] commutation of the royalty payments under the contract of 1935, producing ordinary income to Rainier. This, your Honor, is not necessarily in conflict with the government's position in the Seattle Brewing & Malting Company case, because Seattle Brewing & Malting Company obtained for a lump sum payment a right to use a trade name for an indefinite period of time. Hence no basis for a deduction has been established insofar as the Seattle Brewing & Malting Company case is concerned. We refer, your Honor, in support of that position, to Whitman & Sons, 11 BTA 1192.

Our next position, your Honor, is that there was no sale of a capital asset, because Rainier still owned a title and property in the trade mark and the trade name "Rainier" and "Tacoma," and good will, if any, the allotment to Seattle (formerly Century) being in the nature of a perpetual license, and is similar to a transaction such as those considered in Clifford Goldsmith v. Commissioner, 143 Fed. (2d) 466, certiorari denied 323 U.S. 774, and M. Whitmark & Sons v. Pastine Amusement Co., 298 Fed. 470, affirmed, Fourth Circuit, 2 Fed. (2d) 1020.

Our next position, your Honor, is that whatever good will, and so forth, Seattle owned in 1913, migrated in 1915 with the advent of statewide prohibition. Seattle Brewing and Malting Company had abandoned its plant in Washington as a brewery at that time, and as we understand, it was never [115] used again by Seattle or its successors as a brewery.

In 1916 Rainier Brewing Company of Washington took over the operations in San Francisco, where the beer was manufactured under the name of Rainier Brewing Company, Seattle Brewing & Malting Company to be entitled to all of Rainier's profits.

If, after 1916, Rainier beer was sold under the name of Rainier Brewing Company, it would appear that there are grounds for contending that whatever good will Seattle Brewing & Malting Company of West Virginia had at that time was lost by disuse.

The next position: It is the government's theory with respect to Section 721 of the Internal Revenue Code, "Abnormal Income," is that since the transaction of 1940 was a commutation of the royalty payments that Seattle would otherwise have made in the future, the income must fall into 1940. If the circumstances had been such that there was a commutation of payments for a specified future time, then there would be no grounds of allocating over such term. Since here the commutation is for an indefinite time, intended to be perpetual, it would be purely speculation to allocate over a future time.

Your Honor please, it might be right at this point to set out clearly that under your view of this case, the only thing transferred was the sole and exclusive and perpetual right to use the trade name "Rainier" and "Tacoma" in the [116] State of Washington and Territory of Alaska, and to market and manufacture beer under that name and that name alone, and when we come to get the March 1, 1913

value, we have to stick to the sale of that trade name alone.

Your Honor please, it is always a very good idea to go right back to the deficiency Notice and what the Deficiency Commissioner said in his Deficiency Notice.

Regarding the $1,000,000 received by Rainier Brewing Company, the Commissioner stated in his Deficiency Notice as follows:

> "(a) In the taxable year you received a payment of One Million Dollars ($1,000,000) from the Century Brewing Association under a contract executed in 1935, whereby you granted to Century Brewing Company a license to use trade names held by you in connection with the marketing of beer, ale, and other alcoholic liquors made from malt in the State of Washington and the Territory of Alaska. No income from such payment was reported in your return for 1940. You contend that the receipt of One Million Dollars ($1,000,000) represented the proceeds of a sale by you of good will and an interest in the trade names, that such good will and trade names have a basis represented by the market value at March 1, 1913, in excess of the proceeds, and that hence no deductible loss was allowable and no taxable gain was reportable.
>
> "It is held that the contract executed in 1935 did [117] not affect the sale of trade names or good will, that the payment of One Million

Dollars ($1,000,000) received by you in 1940 was ordinary income taxable in full without any offset for the claim basis.

"It is further held that since the transaction did not constitute a sale, the income realized in 1940 may not be excluded from excess profits net income under Section 721 of the Internal Revenue Code."

Your Honor please, that is the exact wording of the Deficiency Notice. Obviously in view of Mr. Mackay's opening statement, Seattle Brewing & Malting Company, Docket No. 2265, has a bearing on this subject case.

Incidentally, your Honor, Mr. Mackay and his associates filed a very able and learned brief amicus curiae in that case.

Mr. Mackay: Thank you.

Mr. Neblett: I am glad to make the statement, Mr. Mackay.

The Seattle Brewing case is presently awaiting decision by the Tax Court, having been heard in Seattle before Judge Mellott on October 31st. The years in that case, your Honor, are 1940 and 1941.

In view of the relation between the two cases, I desire to call your Honor's attention to the wording of the Deficiency Notice in the Seattle Brewing & Malting Company [118] case. Said Deficiency Notice reads as follows, for the year 1940, and it is exactly the same for the year 1941, except a different amount of deduction is claimed.

"(a) It is held that you are not entitled

> to amortization of any part of the cost of the perpetual right and privilege to manufacture and market beer and other alcoholic malt beverages under designated trade names and brands purchased in 1940 for One Million Dollars ($1,000,000). The deduction of $56,498.13, which was claimed on your return as amortization of the cost of such perpetual rights and privileges is therefore disallowed and added to the income shown on your return."

The deduction claimed in 1941, your Honor, was $142,821.04.

The ultimate question, therefore, in the Seattle Brewing and Malting Company, Docket No. 2265, is not the same as the question in the instant case. The question there, your Honor, was whether Seattle Brewing & Malting Company was entitled to deduct from income for '40 and '41 any portion of the contract price of $1,000,000. It agreed in 1940 to thereafter pay Rainier Brewing Company, Incorporated, of San Francisco, California, in order to terminate all royalties thereafter payable under their existing agreement of April 23, 1935, by virtue of which contract and consideration Seattle Brewing & Malting Company acquired the exclusive and perpetual right [119] to thereafter manufacture and market beer and other alcoholic malt beverages within the State of Washington and the Territory of Alaska under their trade name "Rainier" and "Tacoma," together with the right to perpetually use it in all trade marks, copyrights, labels or other advertising media thereafter adopted or

used by Rainier Brewing Company in connection with such products. Rainier's agreements, your Honor, was not to compete in that business in the assigned territory.

Respondent took the position, in other words, in the Seattle case that the sum paid or agreed to be paid by Seattle Brewing & Malting upon exercising the option in 1940 under its contract with Rainier Corporation for the several intangible properties and property rights acquired under such contract, constituted a capital expenditure, no part of which may be deducted as an expense or otherwise, and, second, that Seattle, by exercising the option in 1940, converted an existing contract from a royalty basis to a capital transaction.

We further took the position in that case, your Honor, that deductions are not allowable as a matter of right by statutory grace, and may be permitted only where specifically authorized by statute. Respondent made an alternative contention in the case, which is not material here.

Additionally, your Honor, Respondent took the further position in the Seattle Brewing & Malting Company case that irrespective of whether the transfer of the right, and [120] soforth, constituted a capital transaction or a license, Seattle Brewing & Malting Company would not be entitled to a deduction because, first, the $1,000,000 payment had no relation to production, and second, the right was of indeterminate life.

Those two points alone, your Honor, were fatal to Petitioner's contention in this Seattle Brewing

& Malting case, irrespective of whether the transaction could be called a capital transaction or a license.

Your Honor please, that constitutes briefly the position taken by the Respondent in the Seattle Brewing and Malting Company case. We might have been wrong in our position up there, your Honor, and in order to protect the revenues, Respondent is now contending and will put into this record all of the evidence he can find bearing on this question, whether it helps or hurts, with respect to the issue here.

In the instant case we shall take the position that Seattle Brewing was merely a licensee, and that insofar as Rainier Brewing is concerned, no sale occurred so as to constitute a capital transaction, which position is consistent with the Deficiency Notice in this case, your Honor, that we read into the record.

I think it may be properly pointed out, your Honor, that the taxability of amounts received by Rainier and deductions [121] claimed by Seattle are not measured or determined by the same statutory rules. There is no necessary reciprocal relation between the two. In other words, your Honor, the Respondent can consistently win both of these cases, irrespective of whether the assets transferred are called a capital asset or a license. The transfer of the rights could very properly be a capital transaction insofar as Seattle Brewing & Malting is concerned, and ordinary income to Rainier Brewing Company.

It can very properly be argued that the sale of the right by Rainier was merely the sale of its stock in trade, and for that reason ordinary income.

For example, your Honor, an architect draws plans for a building. Insofar as the owner of the building is concerned, it is a capital transaction, but he, the architect, gets his ordinary income. Under the contract of April 23, 1935, Seattle Brewing & Malting could have continued to pay royalties. There was no obligation requiring Seattle Brewing & Malting Company to exercise the option to terminate the royalties. In fact, it can be argued that Seattle Brewing got very little of anything that it did not already have by exercising the option. There is no occasion for Seattle Brewing Company to exercise the option in order to keep on using the name "Rainier" in the State of Washington and the Territory of Alaska. [122]

True, by exercising the option, Seattle Brewing & Malting has substantially cut down future payments of royalties.

Your Honor please, right at that point, when the contract was entered into in 1935, Seattle Brewing was not so sure that they could make a go of that name, apparently, so they thought they would take an option, after trying it out for five years to see whether they really wanted to purchase it, and after working with it for five years and making quite a little money, they decided they would purchase it for the $1,000,000 we are talking about here. There is no doubt about the fact that Seattle Brewing acquired a right in perpetuity when it

entered into the contract of April 23, 1935, as long as it did not default under the contract.

Your Honor please, if at any time since Seattle had defaulted under that contract, the properties and other things would have gone back to Rainier, the seller, the Petitioner here. Only in the case of default was there a referrer to Rainier of the assets transferred.

Mr. Mackay has adverted to several other facts, your Honor, so I will not repeat all the facts. I am just going to repeat enough facts to develop our theory and to present the picture in a little fuller detail.

As above stated, and as pointed out by opposing counsel, on April 23, 1935, Rainier Brewing Company, Inc., a [123] California corporation, entered into a contract with Century Brewing Association, a Washington corporation, the latter corporation now known as "Seattle Brewing & Malting Company." This contract recited that Rainier was engaged in manufacturing beer, ale and other alcoholic malt beverages, with plants located at San Francisco, California and Seattle, Washington, and in marketing said products in eleven western states, the Territory of Alaska and Hawaii and elsewhere; that Century Brewing Association was engaged in the manufacture of beer and other malt products, with a plant at Seattle, Washington, and in marketing said products in the States of Washington and Oregon, the Territory of Alaska and elsewhere.

For many years Rainier had sold and marketed its product in Washington and Alaska under the

trade name and brands of "Rainier" and "Tacoma." Seattle Brewing & Malting Company desired to acquire the plant and certain other of Rainier's personal property in Seattle, Washington, and to secure the sole and exclusive and perpetual right and privilege of manufacturing and marketing beer, ale and other alcoholic beverages under said trade name within the State of Washington and the Territory of Alaska.

These are the provisions in the contract.

Incidentally, your Honor, I picked some of that wording from Mr. Mackay's able brief amicus curiae in the Seattle case. [124]

That Rainier was willing to sell this plant and personal property and to grant said perpetual right and franchise upon the terms and conditions set forth in the agreement.

Pursuant to the terms of the contract, Rainier transferred and Seattle Company acquired the Seattle plant for the sum of $250,000 and certain personal property, namely, payrolls and containers, cases, sales material, office fixtures and equipment, and all beer on hand.

Paragraph 7 of the contract is as follows:

> "(7) Rainier hereby grants to Century the sole and exclusive perpetual right and license to manufacture and market beer, ale and other alcoholic malt beverages within the State of Washington and the Territory of Alaska under the trade name and brands of 'Rainier' and 'Tacoma,' together with the right to use within

> said State and Territory any and all copyrights, trade marks, labels or other advertising media adopted or used by Rainier in connection with its beer, ale or other alcoholic malt beverages.''

In consideration of the right thus granted Petitioner, Seattle agreed to pay Rainier a royalty of seventy-five cents per barrel on all such beverages sold in Washington and Alaska under the trade name "Rainier" and "Tacoma," up to 125,000 barrels annually, and a royalty of eighty cents per barrel on all such beverages sold in excess of 125,000 barrels [125] per year. The minimum royalty, however, was to be the sum of $75,000 per year.

The contract further provided in paragraph 13, which is extremely important, your Honor, in this case:

> "It is understood and agreed by and between the parties hereto that at any time after this agreement has been in force for five years, Century shall have the right and option of electing to terminate all royalties thereafter payable hereunder by notifying Rainier of its election to do so,——"

Notice those words "terminate all royalties," your Honor.

> "——and by executing and delivering to Rainier the promissory note of Century aggregating in principal amount the sum of One Million Dollars ($1,000,000), dated as of the date

of the exercise of such option, bearing interest from date at the rate of five per cent (5%) per annum, which said promissory note shall be divided into five (5) equal maturities, and shall be payable respectively on or before one (1), two (2), three (3), four (4), five (5) years after the date thereof."

That option, your Honor, was exercised on July 1, 1940.

To sum up very briefly the more important clauses in that contract, because after all the four corners of that [126] contract will probably determine the question:

1. As I said before, Century agreed to buy from Rainier, for the sum of $250,000, the land and building comprising a brewery in Seattle then owned by Rainier, but which had been operated very little.

2. Century also agreed to buy from Rainier for stated amounts certain bottles, cases and other equipment, and all beer in retail dealers' hands as of July 1, 1935.

3. Rainier granted to Century the exclusive right to manufacture and market beer under the trade name as I have previously mentioned.

4. Rainier agreed that during the time this agreement remains in force, it would not manufacture, sell or distribute within the territory covered by the agreement, directly or indirectly enter into competition with Century in said territory, it being agreed, however, that Rainier could retain the exclusive right to manufacture, sell and distribute

non-alcoholic beverages within such territory under the trade name "Rainier" and "Tacoma."

Your Honor, right there is an interesting point, that even though Rainier gave to Seattle Brewing and Malting Company the perpetual right to sell beer and alcoholic malt beverages in the State of Washington and Territory of Alaska, Rainier retained the right to sell non-alcoholic beverages in the State of Washington and the Territory of Alaska under the [127] trade name "Rainier." That is a very important point in the case, your Honor.

Next, Rainier agreed that any time after this agreement had been in force for five years, Century could have the right and option of electing to terminate all royalties thereafter by exercising and delivering to Rainier promissory notes aggregating $1,000,000, payable in one, two, three, four, five years.

Next, Century agreed, during the period this agreement remained in force, it would purchase from Rainier all of the malt required by it to manufacture beer and ale sold under the trade name "Rainier" and "Tacoma." That was paragraph 14 of the agreement.

Century agreed to use its best effort to increase the volume of sales under the trade name "Rainier" and "Tacoma," so that these sales would equal the volume of sales of all other such products manufactured and sold by Century within the territory covered by the agreement, and would expend in advertising Rainier and Tacoma beer and ale an amount equal to the sum expended by it in adver-

tising all other beverages manufactured and sold by Century within that territory.

In other words, your Honor, Century had an agreement with Rainier that they would spend money advertising the name "Rainier," and I take it if a default had occurred there, [128] these profits would have reverted back to Rainier.

Next, Century agreed that in the event it should fail to carry out the terms of the agreement or make the payments agreed upon, and such failure should continue for thirty days, such failure should be and become an event of default, and that Rainier could cancel the agreement by written notice to Century. That is paragraph 22.

No right of Century under this contract could be assigned without the written consent of Rainier first had and obtained. That is paragraph 24, your Honor.

When you buy something, and it belongs to you, you can sell it, give it away if you want to, but under this contract Seattle Brewing & Malting Company could not assign it to anybody in the world unless they came down here and got Rainier's consent. That makes it look much more like a license than it would a sale.

The contract further provided that should Century at any time be prevented from manufacturing and selling beer, ale or other alcoholic beverages under the trade name "Rainier" and "Tacoma" in a quantity equal to at least 52,000 barrels annually due to governmental regulations, and incidentally, your Honor, general prohibition laws adopted by

the United States of America or the State of Washington. Your Honor, even in 1935 there was a fear lurking that prohibition might come back again. It had quite a bearing on [129] 1913, when the evidence will show that the whiskey business was in a death struggle to stay in business.

Mr. Mackay: This is not whiskey. I object to that.

Mr. Neblett: Well, the beer business. They both are respectable businesses, Mr. Mackay.

Mr. Mackay: Thank you.

Mr. Neblett: Your Honor please, it is evidenced from the terms of the contract just summarized between Rainier and Century that it included rights and privileges of a substantial value other than the right to use the trade name "Rainier" in the State of Washington and the Territory of Alaska. For example, (1) such as Century's obligation to buy malt from Rainier, (2) elimination of competition by Rainier, (3) the obligation on Century's part to expand for advertising, and (4) the obligation on Century's part to purchase the plant of Rainier for $250,000.

Incidentally, your Honor, I have a copy of the original contract here, and it is very interesting sometimes to notice that with respect to the sale of the property itself, the $250,000 transaction, that contract says "Purchase Agreement."

With respect to the sale of the right to do business in the State of Washington and Territory of Alaska, that contract says "License Agreement."

Your Honor please, as we view the issue as defined by the pleadings in this case, the sole and exclusive and perpetual right to manufacture and market beer, ale and other alcoholic beverages under the trade name "Rainier" and "Tacoma" in the State of Washington and Territory of Alaska is the only item to be valued as of March 1, 1913, assuming they are entitled to use a March 1, 1913, value. We will come to that a little later, your Honor.

In short, the March 1, 1913, value of that right, and that right alone entered into the determination of Rainier taxable gain from the transfer in 1940 of the right under consideration in this case. Obviously the amount paid for the right in 1940 by Seattle Brewing would not be any indication of this same right's value in 1913.

The evidence will show, your Honor, that the conditions in 1913, just prior to state-wide prohibition and national prohibition, were entirely different than they were in 1940. The circumstances are so entirely different.

In any event, the amount to be considered as having been paid in 1940 for the elimination of competition would first have to be segregated from the total amount paid, and a determination made of the amount actually paid for the right to use the name "Rainier" before any comparison could be made between the 1913 value of the right with its value in 1940.

Therefore, your Honor, the crucial question is whether Petitioner is entitled to use the March 1, 1913, value of the right, and if so, has it the right

to manufacture and market beer in the assigned territory under the trade name of "Rainier" and "Tacoma"? In other words, your Honor, is Petitioner entitled to use that right, and if so, what was its March 1, 1913, value?

The question after all comes down to: What a prospective buyer as of March 1, 1913, would have been justified in paying for that right, and that right alone, separate and apart from any of the other assets of the business of which it formed a part, and on the basis of the profits which this prospective buyer might expect to receive in subsequent years from the right that he then acquired.

In other words, your Honor, this contract of 1935 had seven or eight things in there that had nothing to do with the sale of that right. Somewhere, somehow, Petitioner must segregate it out and show what that right, and that right alone, to manufacture and market beer in the State of Washington and Territory of Alaska, what was the value of that?

Your Honor please, the test is, what a willing seller will take and what a willing buyer will pay, both having full knowledge of the facts, and neither being under compulsion to buy or sell.

Summarizing, your Honor, two distinct facts must [132] be kept in mind in this case, we think.

First, the question at issue is the market value as of March 1, 1913, assuming Petitioner is allowed to use that value of only the exclusive perpetual right and license to manufacture and market beer within the State of Washington and the Territory of Alaska.

Second, that conditions affecting the value of this right in 1913 were entirely different than in 1940, and

Third, Century in 1940, in consideration for the amount of $1,000,000 then paid, received in addition to the right in question other rights and privileges at that time, but which rights did not in any way form a part of the March 1, 1913, value of the right transferred by Petitioner in 1940.

The evidence will show that in 1913 the Seattle Brewing & Malting Company, then owner of the right in question, owned and also operated a brewery in Seattle, in which it had an investment of approximately $2,900,000. Your Honor, I am trying to be as accurate as I can. That figure may be varied a little. It may be $2,900,000, it may be a little less or it may be a little more. Not including intangibles or investments in other properties, 82 per cent of its total net income was received from sales of beer and ale in the State of Washington under the trade name "Rainier."

Since the evidence will show that a purchaser in [133] 1913 of the rights to sell beer and ale in the State of Washington under the trade name "Rainier" would have also purchased Seattle's brewery, of a value of practically $3,000,000, it must follow that after the sale of that right the Seattle Brewing & Malting Company would have commenced to manufacture and market beer and ale under another name.

In other words, your Honor, if I had gone up there and bought the name, unless I could buy

Seattle Brewing & Malting Company's $3,000,000 brewery, what good would the name do me? Seattle Brewing & Malting Company could step out and sell beer under any other name, and there would be nothing the buyer could do.

The evidence will show that the Rainier Brewing Company, the seller, in 1940 was then operating a brewery in San Francisco, and could therefore dispose of the right in the State of Washington and Territory of Alaska without disrupting its other business at all.

Your Honor please, the contract of April 23, 1935, shows that no good will was transferred to Seattle. In fact, the agreement specifies that Seattle must protect the good will of Rainier Brewing Company in the quality of beer manufactured, and by their advertising, and those provisions are in force today, your Honor, under our theory of this contract. Therefore, the good will of Rainier Brewing Company [134] was a general thing which was retained under the 1935 agreement, and Rainier Brewing Company still retained it. All they sold was a little part (I don't know how they could figure it out, your Honor) of the good will, if they could call it "good will", some sort of intangible value, when they sold the right to use it in the State of Washington and the Territory of Alaska.

In 1913, however, the sales of Rainier Beer, your Honor, (and the evidence will show in some detail) in the State of Washington were by far the larger part of the entire business of the Seattle Brewing and Malting Company. I base that statement on

certain information Petitioner submitted, and I think Mr. Mackay adverted to that in his opening statement.

The agreement under which the right was purchased in 1940 provides that the seller of the right will not directly or indirectly enter into competition with the buyer. Thus, the owner of the right in 1913 could not have made such an agreement without abandoning a brewery worth approximately somewhere between $2,500,000 and $3,000,000. The evidence will show, your Honor, that no such agreement could have been made in 1913.

Additionally, a prospective purchaser of this right in 1913 would therefore have had to face the fact that the volume of sales he might expect would be only from patrons [135] who thought so highly of the name "Rainier" that they would buy no beer or ale sold under any other name, and the further fact that the prior owner of that right was an old and well established organization, and holding a control over a large number of what are called in the beer business, your Honor, "captive saloons", which actually enable it to dictate the brand of beer such saloons might sell if they intended to remain in business as competitors.

The evidence will show, your Honor, that this situation would have a decidedly adverse effect upon the amount a prospective purchaser might otherwise have paid for the right in question.

In other words, your Honor, I think about 80 per cent of the brewery business in 1913 (and it is probably true today) would finance these saloons,

and naturally, if the brewery was financing the saloon, the saloon would have to sell the brand of beer the brewery put out, irrespective of its name.

The evidence will show, your Honor, that Seattle, with a $3,000,000 going concern up there, could have put up a beer under a good old Indian name, "Snoqualmie Falls", for instance, and the man that sold beer right along under the name "Rainier" would not have had anything of value.

Regarding control of saloons in the State of Washington, which would have enabled the seller to remain in [136] competition with the buyer of that right, the evidence will show that the brewers in the State of Washington and elsewhere actually took out and held licenses for a large number of the saloons then in business in that State, and that these saloons very naturally and unquestionably promoted the sale of the brand of beer manufactured by the brewery which held their license. As a matter of fact, your Honor, 80 per cent of the saloons were sold throughout the United States in 1913.

Further, the evidence will show that the Seattle Brewing & Malting Company could, in 1913, after selling the right to use the trade name "Rainier" to another brewery, establish a market for its product under another trade name, for example, and have substantially reduced the volume of sales of Rainier beer, and that any prospective purchaser of the right would have been aware of that fact and given it consideration in any offer made in 1913 for the right to use the trade name of "Rainier" in

the State of Washington and the Territory of Alaska.

The evidence will further show that a purchaser of the right in 1913, before deriving any profit from the sale of beer and ale under the trade name "Rainier", would have to make allowance for the manufacture of these products either by a brewery owned by the purchaser, which would require a reasonable return on the investment in the brewery before any profits could be attributable to the name "Rainier," or by payment of the cost of manufacture to some other brewery. That is the only way a purchaser of that name could have operated in Washington in 1913.

The evidence will show that the earnings of the Seattle Brewing & Malting Company for the five-year period prior to 1913 were sufficient, according to Petitioner's competition, to pay eight per cent return on investment in plant at fifteen per cent on the claimed value of good will, but since another brewery would be required for the manufacture of Rainier beer and ale by the buyer of the right to use that trade name, only that part of the profit from the sale above would be a reasonable return when an acquired investment in the additional plant should be included in the computation of the value of that intangible, which would substantially reduce the Petitioner's formula, which would substantially reduce his value.

Next, the evidence will show, your Honor, that as of March 1, 1913, there was a definite possibility of state-wide prohibition becoming effective in the

State of Washington. In fact, such a possibility had become generally recognized throughout the State of Washington and other states in the Union. The evidence will show that a prospective purchaser of the right in question would have been aware of that possibility. [138]

The evidence will further show that prohibition of the manufacture and sale of intoxicating liquors, including beer and ale, in the State of Washington, became effective January 1, 1916, following the election on November 3, 1914, which was held as a result of a petition filed January 8, 1914, containing the number of signatures required by the initiative and referendum measure which had been passed by the Assembly of Washington and had become effective prior to 1913.

Incidentally, your Honor, those figures are quite interesting. On March 12, 1909, that local option was approved in the State of Washington. In 1910 woman sufferage was adopted in the State of Washington, and I think the evidence will show that the prohibitionists thought that the interests supporting woman sufferage would be supporting prohibition. In 1911 woman sufferage was adopted in California, and as I say, on January 8, 1914, the initiative and referendum measure No. 3 was passed in Washington.

Right along that line, Respondent believes the evidence will show that in 1910 approximately 1650 saloons were operating in the State of Washington. By 1912, 350 saloons had been abolished, and by 1913 a total of 572 saloons had been abolished, leav-

ing 1100 saloons still operating in the State of Washington in 1913. Your Honor please, that is a pretty good trend, and when you are spotting trends, that [139] looks like prohibition was coming along pretty fast.

The evidence will show further that the saloon keepers would buy beer from the brewers that financed them, irrespective of the name of the beer being sold. I have already covered that, your Honor.

In 1913 there had been sustained agitation on the liquor situation for several years, and although the dry forces had been unable to secure the passage in the State Assembly of any prohibition act, they had secured in 1910 passage of the woman sufferage, which they considered helpful to their cause as, rightly or wrongly, they thought the large majority of the women of the State would be in favor of prohibition, and also secure the passage of the prohibition and referendum measure which allowed them to secure the passage of a local measure which had designated each city and county of the State of Washington a unit empowered to hold an election, and if a majority of the voters of the city and county failed to vote for license, the prohibition of the sale of intoxicating liquors in that city or county would become effective ninety days after election.

We will show you no licensed territory in the State of Washington in 1913.

The evidence will show further that a number of the cities and counties of the State of Washington had already held elections and had voted for local

prohibition prior [140] to 1913, and that the effect of those elections had been felt by the brewers of the State of Washington. In other words, in 1913, your Honor, prohibition was winning the West. The situation was becoming acute for the brewers in 1913. That will be the substance of the Respondent's evidence along that line.

Further, in addition to the uncertainty as to the actual market value, if any, in 1913 of the right under consideration, there is also a question as to whether the basis for determination of a taxable gain from the sale of the right sold in 1940 is in fact a March 1, 1913, value of the right then owned by the Seattle Brewing & Malting Company.

Your Honor please (and this is a very important point from the Respondent's standpoint), I am referring now to the Haberle Springs case, your Honor. I might state the name of that case, just for the record. Haberle Crystal Springs Brewing Company v. Clarke 280 U.S. 384 L.A.F.T.R. 10267. That case held, your Honor, that petitioners were not entitled to deduction for obsolescence of good will, Justice Holmes writing a very interesting opinion, that the brewery business was extinguished by the National Prohibition Act.

The evidence will show in support of that theory, your Honor, that prohibition became effective in the State of Washington January 1, 1916, and national prohibition January [141] 16, 1920, and for more than fifteen years the manufacture and sale of alcoholic beverages in that State was absolutely prohibited, and during that entire period the right

to manufacture and market alcoholic malt beverages under the trade name "Rainier" very certainly had no market value. Your Honor please, during that period of time the right to market beer was dead.

If, therefore, such value, if any, as the right in question may have had as of March 1, 1913, entirely disappeared by disuse or was extinguished for any other reason, and if that right was worthless for a period of fifteen years or more, can it now be said that the value of that right remained only dormant, and is the proper basis for the sale in 1940, or is the value of that right sold in 1940 something which has been created since the repeal of prohibition? Obviously, your Honor, that very fact, that they put that five-year clause in that agreement of April, 1935, shows that this value here was created after the repeal of prohibition. Therefore the evidence will show that a very substantial part, if not all of it, your Honor, of the value which this right had in 1940, namely, the $1,000,000 was created during the five years from 1935 to 1940. As was above stated, during that period of time Seattle Brewing & Malting Company had to keep the advertising up and make some other provisions. [142]

The evidence will further show that Seattle Brewing & Malting commenced in 1935, made large expenditures for advertising the name "Rainier." In fact, the agreement of April 23, 1935, required Seattle Brewing & Malting to make such expenditures for those purposes.

Just one other thought and Respondent is through with his opening statement, your Honor.

Stipulation No. 3 is not in, but back there in the early years, 1918 and 1919, Respondent allowed Petitioner, then Seattle Brewing & Malting Company, some obsolescence for good will. The Supreme Court came along and said you could not do that, you could not have obsolescence of good will, especially when a business had been destroyed by law. I think they allowed them $406,680.

The result of that, even though it was an unlawful allowance, your Honor, Petitioner has a tax benefit in the year 1918-19. In 1918 the tax benefit was $78,983.92, and in 1919 the tax benefit was $59,153.48, totalling $138,137.40.

Your Honor please, I call that to your Honor's attention at this point, because, assuming you should find that it is entitled to use its March 1, 1913, value, and that it had a value of $138,137.40, then the tax benefit they got for those two years back there would cancel out the March 1, 1913, value, so Petitioner would not have anything, in any [143] event.

Your Honor, please, that briefly covers the Respondent's theories, position and what he will hope to show in this case.

The Court: Mr. Mackay?

Mr. Mackay: Your Honor please, counsel has been very cooperative in trying to shorten the trial of this case, and as a result we have entered into several stipulations.

At this time I should like to offer in evidence a stipulation which has to do with the various non-

taxable reorganizations wherein we agreed that they are non-taxable reorganizations.

The Court: May I ask if you are going to designate these various stipulations by some number, or are you going to call them the "first stipulation," and so on?

Mr. Mackay: Yes. We ought to call this "No. 1," please, if we may.

The Court: Have you so designated them?

Mr. Mackay: Will you please write "No. 1" on there? We have others, but we failed to do so on No. 1.

The Clerk: Yes.

The Court: That agreed statement of facts which is designated as Stipulation No. 1 is received and made part of the record. [144]

Mr. Mackay: Now, with your Honor's permission, I shall submit Stipulation No. 2, and for the record will state that it merely shows the royalties that were paid by Century during the fiscal years ending from July 1, 1935 to June 30, 1940, and also the number of barrels of beer that were sold during that time.

The Court: Stipulation No. 2 is received and made part of the record.

Mr. Mackay: I should like to offer now Stipulation No. 3, which has to do with the last point mentioned by counsel for the Respondent, relating to the so-called "tax benefits for 1919 and 1918.

The Court: Stipulation No. 3 is received and made part of the record.

Mr. Mackay: Now, if your Honor please, I

should like to offer as Petitioner's Exhibit 1 a photostatic copy of the contract which has been referred to here, which is dated April 23, 1935, between Rainier Brewing Company and Century Brewing Company.

Mr. Neblett: No objection, your Honor.

The Court: Mr. Mackay, are you offering that as Petitioner's Exhibit 1?

Mr. Mackay: Yes, your Honor.

The Court: Without objection that is received as Petitioner's Exhibit 1. [145]

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 1.)

[Petitioner's Exhibit No. 1 appears in Book of Exhibits.]

Mr. Mackay: Your Honor please, I should like to offer as Petitioner's Exhibit 2 a photostatic copy of a supplemental agreement between the same parties dated July 1, 1935.

The Court: Received without any objection?

Mr. Neblett: That is right; no objection.

The Court: It will be received as Exhibit 2.

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 2.)

[Petitioner's Exhibit No. 2 appears in Book of Exhibits.]

Mr. Mackay: I should like to offer as Petition-

er's Exhibit 3 a supplemental agreement between the same parties dated July 18, 1935.

The Court: Without objection, that is received as Exhibit 3.

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 3.)

[Petitioner's Exhibit No. 3 appears in Book of Exhibits.]

Mr. Mackay: I should like to offer in as Petitioner's Exhibit 4 a deed dated July 18, 1935, transferring the Washington plant from Rainier to Seattle.

Mr. Neblett: No objection.

The Court: Received as Exhibit 4.

(The document referred to was received in evidence and marked Petitioner's' Exhibit No. 4.)

[Petitioner's Exhibit No. 4 appears in Book of Exhibits.] [146]

Mr. Mackay: I should like to offer in, your Honor please, a copy of the mortgage dated July 19, 1935, from Seattle Brewing & Malting Company to Rainier, securing unpaid balance of $50,000.

Mr. Neblett: No objection.

The Court: Received as Exhibit 5.

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 5.)

[Petitioner's Exhibit No. 5 appears in Book of Exhibits.]

Mr. Mackay: Your Honor please, I should like to offer as the next exhibit for Petitioner an agreement which I think may be hereinafter called a "trust indenture," dated July 19, 1935, between Seattle Brewing & Malting Company, formerly Century Brewing Company, and First National Bank of Seattle and Rainier Brewing Company.

Mr. Neblett: No objection.

The Court: Received as Exhibit 6.

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 6.)

[Petitioner's Exhibit No. 6 appears in Book of Exhibits.]

Mr. Mackay: Your Honor please, the next exhibit I should like to offer is a supplemental agreement dated November 27, 1935, between the same parties.

Mr. Neblett: No objection.

The Court: Received as Exhibit 7.

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 7.)

[Petitioner's Exhibit No. 7 appears in Book of Exhibits.] [147]

Mr. Mackay: Your Honor please, I should like to offer as the next exhibit a letter dated July 1, 1940, from Seattle Brewing & Malting Company to Rainier Brewing Company, exercising the option that we have just discussed.

Mr. Neblett: No objection.

The Court: Received as Exhibit 8.

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 8.)

[Petitioner's Exhibit No. 8 appears in Book of Exhibits.]

Mr. Mackay: I might explain that attached to that exhibit is a letter to the Anglo California National Bank dated July 1, 1945, and also a promissory note.

Your Honor please, I would like to offer as Petitioner's next exhibit a copy of a Satisfaction of Mortgage dated February 2, 1942, relating to the mortgage dated July 19, 1935.

Mr. Neblett: No objection.

The Court: Received as Exhibit 9.

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 9.)

[Petitioner's Exhibit No. 9 appears in Book of Exhibits.]

Mr. Mackay: Your Honor please, the next exhibit I would like to present is a photostatic copy of a letter dated April 11, 1942, from Seattle Brewing & Malting Company to Mr. Joseph Goldie, President of the Rainier Brewing Company.

Mr. Neblett: Mr. Mackay, I had not seen a copy of this letter. What is the purpose of this

testimony? It [148] refers to the fact that the State of Idaho has been added to the contract.

Mr. Mackay: That is all.

Mr. Neblett: No objections, your Honor.

The Court: Received as Exhibit 10.

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 10.)

[Petitioner's Exhibit No. 10 appears in Book of Exhibits.]

Mr. Mackay: I should like to offer a photostatic copy of a letter dated April 13, 1942, from Rainier Brewing Company to the then Seattle Brewing & Malting Company.

Mr. Neblett: No objection, your Honor.

The Court: Received as Exhibit 11.

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 11.)

[Petitioner's Exhibit No. 11 appears in Book of Exhibits.]

Mr. Mackay: Your Honor please, I offer in evidence as the next exhibit a photostatic copy of a letter dated November 25, 1942, addressed to the Rainier Brewing Company from Seattle Brewing & Malting Company, which has a copy of a letter dated November 25, 1942, to Seattle Brewing & Malting Company from Rainier, and also a copy of a letter dated November 25, 1940, to the First Trust

National Bank of Seattle, from Rainier Brewing Company, and also a copy of a trust indenture, 25th day of November, 1942.

Mr. Neblett: If your Honor will just bear with us for a second. I think this is all right, but I will have to [149] make a little check.

The Court: Mr. Mackay, you have a good many exhibits to offer and I think the reporter should have a rest now. I am sure the reporter did a magnificent feat of reporting during those long opening statements, and particularly considering the rapidity of the very fluent Mr. Neblett. I think, in the beginning, we should thank the reporter, and in that connection I am going to ask you to please remember the reporter. I will take a recess every hour or hour and a half.

Mr. Mackay: I think that is quite kind.

(Short recess.)

The Court: An exhibit was offered. It was being checked by Mr. Neblett.

Is there any objection?

Mr. Neblett: No objection.

The Court: Received as Exhibit 12.

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 12.)

[Petitioner's Exhibit No. 12 appears in Book of Exhibits.]

Mr. Mackay: Now, if your Honor please, I should like to offer in as the next exhibit of Peti-

tioner a consolidated balance sheet for the fiscal years ending June 30, 1907, 1908, 1909, 1910, 1911 and 1912.

Mr. Neblett: Mr. Mackay, I notice——

Mr. Mackay: That is the same copy that I gave you. [150] I mean they are copies exactly.

Mr. Neblett: I notice that you only go to 1912.

Mr. Mackay: We are coming down with some others to go into '13 and '14.

Mr. Neblett: With that understanding, your Honor, no objection.

The Court: Received as Exhibit 13.

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 13.)

[Petitioner's Exhibit No. 13 appears in Book of Exhibits.]

Mr. Mackay: The next exhibit, if your Honor please, I should like to offer is a statement of income and earned surplus for the same years, beginning June 30, 1908 and ending June 30, 1912.

Mr. Neblett: I just wanted to make sure that you are bringing that down to 1913.

Mr. Mackay: Yes, I am.

Mr. Neblett: With that understanding on it, no objection.

The Court: Received as Exhibit 14.

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 14.)

[Petitioner's Exhibit No. 14 appears in Book of Exhibits.]

Mr. Mackay: The next one I should like to offer, if your Honor please, is a statement of sales, costs of goods sold and gross profit on sales for the years during June 30, 1908 to and including June 30, 1912. [151]

Mr. Neblett: With the same understanding, we have no objection, your Honor.

The Court: Received as Exhibit 15.

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 15.)

[Petitioner's Exhibit No. 15 appears in Book of Exhibits.]

Mr. Mackay: If your Honor please, I would like to offer the balance sheet of June 30, 1913, which was prepared from the books and checked by the Federal agents.

Mr. Neblett: No objection.

The Court: Received as Exhibit 16.

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 16.)

[Petitioner's Exhibit No. 16 appears in Book of Exhibits.]

Mr. Mackay: If your Honor please, I would like to offer in the photostated copy of the balance sheet, June 30, 1914 to 1915, which has been prepared from the books.

Mr. Neblett: Your Honor please, no objection subject to check. Our agent has not checked this particular sheet.

The Court: You will make note of that, then, that you are going to check Exhibit 17?

Mr. Neblett: Yes, your Honor.

The Court: Received as Exhibit 17, subject to check.

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 17.)

[Petitioner's Exhibit No. 17 appears in Book of Exhibits.]

Mr. Mackay: Now, if your Honor please, I would like [152] to offer the next exhibit, which is called a "Statement of Income and Earned Surplus for the Year Ended June 30, 1914."

Mr. Neblett: We have a copy of that, Mr. Mackay. No objection.

The Court: Received as Exhibit 18.

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 18.)

[Petitioner's Exhibit No. 18 appears in Book of Exhibits.]

Mr. Mackay: If your Honor please, I should to offer now a statement of income and earned surplus for the years ended June 30, 1914 and 1915.

Mr. Neblett: No objection on this, subject to check.

The Court: Received as Exhibit 19, subject to check.

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 19.)

[Petitioner's Exhibit No. 19 appears in Book of Exhibits.]

Mr. Mackay: Then, if your Honor please, I would like to offer a photostatic copy from the books of the Company, which is entitled "Comparative Statement of Sales and Net Profits by Agencies, Beginning with Year Ending June 30, 1903", and it goes down to 1913.

Mr. Neblett: No objection on it, subject to check.

Mr. Mackay: I might state, Mr. Neblett, this is an exact photostatic copy of it, but I don't mind your checking it. [153]

The Court: Received as Exhibit 20, subject to check.

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 20.)

[Petitioner's Exhibit No. 20 appears in Book of Exhibits.]

Mr. Mackay: If your Honor please, I should now like to offer in as the next exhibit, "Seattle Brewing & Malting Company"; which I might state was the predecessor of this Petitioner, and it is

entitled "Organization Expenses and Purchase of Goodwill as set up through Audited Vouchers".

Mr. Neblett: No objection.

The Court: Received as Exhibit No. 21.

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 21.)

[Petitioner's Exhibit No. 21 appears in Book of Exhibits.]

Mr. Mackay: The next exhibit, your Honor please, that I would like to submit——

Mr. Neblett: Just a minute. Could I interrupt you?

Mr. Mackay: I am sorry.

Mr. Neblett: Could you give us a copy of the last exhibit, Mr. Mackay?

Mr. Mackay: Oh, yes, indeed. (Handing document to counsel.)

The next exhibit is a photostatic copy entitled "Seattle, Novemebr, 1912", and it has to do with a writeoff of good will and some expenses. [154]

Mr. Neblett: No objection. If you will furnish us with a copy, Mr. Mackay?

Mr. Mackay: Oh, yes.

The Court: Received as Exhibit 22.

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 22.)

[Petitioner's Exhibit No. 22 appears in Book of Exhibits.]

Mr. Mackay: The next exhibit I should like to offer, if your Honor please, is entitled "Seattle Brewing & Malting Company, (A Washington Corporation) and Seattle Brewing & Malting Co., (A West Virginia Corporation), earnings by periods from February 1, 1893 to June 30, 1915".

Mr. Neblett: No objection.

Could we be furnished a copy?

Mr. Mackay: Oh, yes indeed.

The Court: Received as Exhibit 23.

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 23.)

[Petitioner's Exhibit No. 23 appears in Book of Exhibits.]

Mr. Mackay: The next one is entitled "Seattle Brewing & Malting Co., Tangible Asset Value as of June 30, 1907 to 1912 inclusive".

Mr. Neblett: No objection, your Honor, subject to check.

The Court: Received as Exhibit 24, subject to check [155]

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 24.)

[Petitioner's Exhibit No. 24 appears in Book of Exhibits.]

Mr. Mackay: Your Honor please, the next exhibit I would like to offer is entitled "Seattle

Brewing & Malting Company Tangible Asset Value of June 30, 1913".

Mr. Neblett: No objection.

T8he Court: Received as Exhibit 25.

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 25.)

[Petitioner's Exhibit No. 25 appears in Book of Exhibits.]

Mr. Mackay: If your Honor please, the next exhibit I should like to offer is a statement showing the dividends paid by periods from February 1, 1893 to June 30, 1915.

Mr. Neblett: No objection.

The Court: Received as Exhibit 26.

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 26.)

[Petitioner's Exhibit No. 26 appears in Book of Exhibits.]

Mr. Mackay: Your Honor please, the next one I should like to offer—it is marked "Exhibit D" here—but it is "Seattle Brewing & Malting Co., Analysis of Construction Property Accounts and Other Fixed Assets, Segregated as to Property Located in State of Washington, and Property Outside the State of Washington".

Mr. Neblett: Covering what period?

Mr. Mackay: Covering the period from 1908 to 1912.

Mr. Neblett: I have no objection, subject to check, [156] your Honor.

The Court: Received as Exhibit 27, subject to check.

(The document referred to was received in evidence and marked Petitioner's Exhibit No. 27.)

[Petitioner's Exhibit No. 27 appears in Book of Exhibits.]

Mr. Mackay: Now, if your Honor please, I have with me here some original prizes that were obtained by the Seattle Brewing & Malting Company, the predecessor of the Petitioner, one at the Exposition Universelle, Paris, in 1900, which is the Grand Prize, and the other one at the Alaska Yukon Pacific Exposition in Seattle in 1909, which was also the Grand Prize. These are prized exhibits of the company, and with your Honor's permission and counsel's permission, I should very much like to not leave these valuable things with the Tax Court, but to submit photographic copies.

Mr.N eblett: Mr. Mackay, are these prizes for Rainier beer, is that it?

Mr. Mackay: No, sir. For beer.

Mr. Neblett: Just what are they?

Mr. Mackay: Rainier Beer. You can see on there, it says, "Seattle Brewing & Malting Company, Gold Medal". I am thinking now of the Alaska Yukon Pacific Exposition. This is the Grand Prize for beer at that Exposition.

The Court: I think Mr. Neblett's point is that

the pictures of the medals of course are good pictures, but they [157] do not tell why the medal was awarded.

Mr. Mackay: I was going to bring that up later with a witness, if your Honor please.

Mr. Neblett: I was trying to find the word "Rainier" written on this thing.

Mr. Mackay: It is there, if you put your glasses on.

Mr. Neblett: I have them on.

Mr. Mackay: I beg your pardon.

(After examining) I think you are right.

The Court: You really are being skeptical about this, Mr. Neblett.

Mr. Neblett: Well, I have tasted Rainier beer, your Honor.

Mr. Mackay: No, you are quite right. "Rainier" is not on there, but I will prove it by a witness. I intended to do that with these prizes for Rainier beer.

Mr. Neblett: I don't think the medals at this point, your Honor, have been sufficiently identified. The word "Rainier" does not appear on them. It might have been "Tacoma" beer.

Mr. Mackay: I will call Mr. Samet. I am sorry, but I thought there would be no objection.

Mr. Neblett: I am sorry.

The Court: Will you step forward, please, to the [158] witness stand?

Whereupon,

RUDOLPH SAMET

called as a witness for and on behalf of the Petitioner, having been first duly sworn, was examined and testified as follows:

Direct Examination

The Clerk: What is your full name?

The Witness: R. Samet.

The Clerk: Your first name?

The Witness: Rudolph.

By Mr. Mackay:

Q. Mr. Samet, you are a resident of Seattle, are you? A. Yes, sir.

Q. Were you connected with the Seattle Brewing & Malting Company at about 1913 and prior thereto? A. Yes, sir.

Q. I show you some medals here which show Alaska Yukon Pacific Exposition at Seattle, 1909, and this one shows the Grand Prize. I will ask what that prize represents.

Mr. Neblett: Your Honor, objected to on the ground that there is nothing here to show yet—of course, that is a preliminary question, I take it?

Mr. Mackay: Yes.

Mr. Neblett: Could I ask the witness a question on Voir Dire?

The Court: Yes.

(Testimony of Rudolph Samet.)

Voir Dire Examination

By Mr. Neblett:

Q. Did you attend this Alaskan Exposition, Mr. Samet? A. I did.

Q. You did? A. Yes, sir.

Q. And the prize which you now have before you was issued to what company?

A. It was given to the Seattle Brewing & Malting Company for the exhibit of their Rainier beer.

Q. For the Rainier beer? A. Yes.

Q. Did Seattle Brewing & Malting Company enter any other beer in that contest? A. No.

Q. They did not? A. No, sir.

Q. Did the Seattle Brewing & Malting Company have any other beer at that time under any other name?

A. Yes. There was a beer called "Bayview".

Q. "Bayview Beer"?

A. Bayview beer, but there was hardly any sold. Very little Bayview has been sold. It was the Rainier beer which [160] was the seller.

Q. Was the Bayview beer entered in this contest in Alaska? A. No, sir.

Q. How does it happen, Mr. Samet, that the name "Rainier" does not appear on that medal?

A. Wait a minute. (After examining) I presume—you know, the prize was given to the manufacturer, not to the product. You know, the manufacturer of anything, he got the prize for manufacturing this kind of beer.

(Testimony of Rudolph Samet.)

Q. Were any other prizes given to other beer people at the same exposition?

A. No, sir. It was the only one at the time exhibiting beer. There was no other.

Q. No other person was exhibiting beer?

A. No other brewery was exhibiting any beer.

Q. Therefore, being the only company, naturally Seattle Brewing & Malting Company got the only prize, is that right?

A. Yes, but you know, like at every exposition, the judges, they tasted and tested the beer, and then they gave you the prize if you deserved it, you know.

Q. My point is that the Seattle Brewing & Malting Company was the only brewery entered into that contest.

A. I think so. Let me see. It is quite a while. Oh, pardon me. Clausen Brewery had one there, too. There was a [161] Clausen Brewery there in Seattle. They had an exhibit.

Q. Did they get a prize?

A. I don't think so. I don't really remember, but I don't think so.

Q. Well, you don't know?

A. You know, this is the Gold Medal, the first prize, we got. Maybe they got second or third, I forget. But, we got the first prize. I remember that.

Mr. Mackay: Mr. Samet, do you know whether the Seattle Brewing & Malting Company received

(Testimony of Rudolph Samet.)
any other gold medals as first prizes for exhibitions of Rainier beer?

The Witness: Yes. We had an exhibit in Dresden, Germany, and we got a Gold Medal there. You talk about competition. We had plenty competition there, but it was so good that they gave us that medal again, or before. It was in Paris, 1900. I did not mention that. At Dresden and at Paris we got Gold Medals, and on some of our labels the medals appear, or used to appear. It is gone.

Mr. Mackay: If your Honor please, I should like to offer these photostats.

The Court: Have you any objection now?

Mr. Neblett: Just one more question.

By Mr. Neblett:

Q. What was the date of the Yukon Exposition?

A. Pardon me? [162]

Q. What was the date of the Yukon Exposition?

A. It was in 1909, I think.

Mr. Neblett: What exhibit are you offering there now?

The Court: Which are you going to offer? There are two medals.

Mr. Mackay: I was going to offer them as a joint exhibit.

Mr. Neblett: I want them separated.

The Court: They should be separated.

On the medal that was given in Paris in 1900, Seattle Brewing & Malting Company appears on the medal, and also the words "Rainier Beer" appears on the medal.

(Testimony of Rudolph Samet.)

Which are you going to offer first?

Mr. Mackay: I shall offer the one in Paris.

The Court: Any objection?

Mr. Neblett: I object to it on the ground, your Honor, that it shows that this Exposition was held in 1900, which is entirely too remote as to any 1913 value. The beer might have been good beer then, but in thirteen years it could have lost its potency.

Mr. Mackay: It is just a matter of following it up.

The Court: It might have lost that fine, pin-point bubble carbonization. [163]

Mr. Neblett: Yes, your Honor.

Mr. Mackay: We submit, your Honor, that it is proper.

The Court: The objection is overruled. I will receive that in evidence as Exhibit 28.

(The photograph referred to was received in evidence and marked Petitioner's Exhibit No. 28.)

[Petitioner's Exhibit No. 28 appears in Book of Exhibits.]

Mr. Mackay: The next exhibit I should like to offer is the photographed copies of the Alaska Yukon Pacific Exposition medal.

Mr. Neblett: Object to it on the ground that the photostatic exhibit relates to the year 1909, I believe. It is too remote in order to base a date.

(Testimony of Rudolph Samet.)

The Court: That is received as Exhibit 29, over the objection.

(The photograph referred to was received in evidence and marked Petitioner's Exhibit No. 29.)

[Petitioner's Exhibit No. 29 appears in Book of Exhibits.]

Direct Examination (Resumed)

By Mr. Mackay:

Q. Mr. Samet, I will ask you, you were General Manager of the Seattle Brewing & Malting Company at that time, weren't you?

A. Yes, sir.

Q. These last two exhibits, one in 1900 and one in 1909, I will ask you if the quality of the beer had been maintained [164] subsequent to the time these prizes were given. A. Yes, sir.

Q. You did not reduce the quality at all?

A. Do what?

Q. You did not reduce the quality?

A. Reduce?

Q. Yes. A. No, sir.

Q. You maintained it?

A. We maintained it, and if we found room for improvement, we improved it.

Q. In 1913 the quality was just the same as it was when you——

Mr. Neblett: Just a minute. Your Honor please, that is objected to on the ground that it is an

(Testimony of Rudolph Samet.)

opinion, and nothing has been shown here to show that Mr. Samet is an expert on beer, nor the quality of beer.

By Mr. Mackay:

Q. Mr. Samet, how long have you been in the brewing business? A. Fifty-seven years.

Q. And during that time have you owned and managed breweries? A. Managed breweries?

Q. Yes. [165]

A. I will tell you: I came to Seattle in 1904. At that time I was Manager of the bottling department, and in 1908—it is so long since—I was made General Manager.

Q. As General Manager, was it your duty to maintain the quality of beer that was being put out under the name "Rainier"?

A. Oh, naturally. You know, the General Manager is in charge of everything; also the brewmaster.

Q. Were you constantly testing it to see whether the quality was maintained? A. I was.

Mr. Mackay: I think he is sufficiently qualified.

The Court: Very well.

The Witness: And I went through the brewing school. You know, even in Europe, before I came out here, I learned the brewing business from the ground up.

By Mr. Mackay:

Q. Are you still in the brewery business?

A. I am still, but in Vancouver, B. C.

Q. But that has nothing to do with the Rainier or Seattle Brewing & Malting Company?

(Testimony of Rudolph Samet.)

A. Nothing whatsoever.

Q. Are you running your own brewery company?

A. Pardon me?

Q. You have your own brewery company? [166]

A. No, it is a corporation.

Q. That is what I mean. A. Yes.

Q. But you are a substantial owner in it, are you? A. Yes.

The Court: Will you ask——

Mr. Mackay: Your Honor please, I should like to ask the witness:

By Mr. Mackay:

Q. Had the quality of Rainier beer in 1913 been maintained at least equal to the quality at the time that these various prizes were given at these various expositions?

A. Yes. It has been maintained. It shows by the sales; they grow.

Mr. Mackay: I think that is all on this.

I will have the witness later, if your Honor please, on some other questions, but I think I would rather not go into that right now.

The Court: You may step down.

The Witness: Thank you.

Mr. Neblett: Could I ask just one question, your Honor, on cross examination?

Cross Examination

By Mr. Neblett:

Q. Mr. Samet, what is the name of your company in Vancouver [167] at the present time?

(Testimony of Rudolph Samet.)

A. Brewers & Distillers of Vancouver, Ltd.

Q. When did you disassociate yourself with the Seattle Brewing & Malting Company?

A. With the Seattle Brewing & Malting Company?

Q. Yes.

A. I am not associated with them now.

Q. When did you disassociate yourself?

A. In 1904. I was then with the Seipp Brewery in Chicago, and E. F. Sweeney brought me out here in 1904, to Seattle.

Q. I am afraid it is not quite clear when you left the Seattle Brewing & Malting Company.

A. When I left them?

Q. Yes.

A. That was after they kicked me out, when the general prohibition started. Then I went North, where the business was legitimate.

Q. Exactly. Do you recall when that was?

A. When I went up North?

Q. Yes. A. In 1923.

Q. 1923 when you went to Vancouver?

A. Yes.

Q. Now, going back to the Paris Exposition.

A. Which one?

Q. The Paris Exposition.

A. The Paris, yes.

Q. Didn't some Eastern brewers have beer entries at that exposition?

A. I presume not only Eastern, but all kinds of European brewers, but you know, I did not go to

(Testimony of Rudolph Samet.)

Paris to overlook it. We had that done through an agent.

Q. You did not attend the Paris Exposition?

A. No, sir, not at Paris.

Mr. Mackay: Is that all?

Mr. Neblett: No. One question.

Mr. Mackay: I am sorry.

Mr. Neblett: May we proceed, your Honor?

The Court: Oh, yes. Excuse me.

By Mr. Neblett:

Q. Mr. Samet, are you aware of the fact that there was statewide prohibition in the State of Washington in 1916?

A. 1st of January, 1916.

Q. January 1, 1916? A. Yes.

Q. What did you do between January 1, 1916 and 1923, when you left for Vancouver?

A. I was Vice President and General Manager of the Rainier Brewing Company here. [169]

Q. In—— A. In San Francisco.

Q. In San Francisco? A. Yes, sir.

Mr. Neblett: That is all.

Mr. Mackay: That is all.

(Witness excused.)

Mr. Mackay: I should like to call at this time, if your Honor please, Mr. Weber.

The Court: Will you come forward, Mr. Weber?